THE SOCIAL COST OF RETRANSMISSION CONSENT REGULATIONS

by

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My name is William P. Rogerson. I am a professor of economics at Northwestern University. In 1998-99 I served as Chief Economist at the Federal Communications Commission ("Commission"). I have published numerous academic articles on industrial organization, regulation, the economics of contracts, and telecommunications and am a Fellow of the Econometric Society. I have served as chairman of the Department of Economics at Northwestern and am currently Co-Director of the Center for the Study of Industrial Organization and Director of the Program for Mathematical Methods in the Social Sciences at Northwestern. A copy of my curriculum vitae is attached at Exhibit 1.

I have been asked by Advance/Newhouse Communications, Cox Communications, and Insight Communications to prepare this study in response to the Commission's inquiry into the impact on competition in the multichannel video programming distribution market of the current retransmission consent rules. *Media Bureau Seeks Comment for Inquiry Required by the Satellite Home Viewer Extension and Reauthorization Act on Rules Affecting Competition in the Television Marketplace*, MB Docket No. 05-28, DA 05-169 (rel. Jan. 25, 2005).

INTRODUCTION

The retransmission consent framework put in place by the 1992 Cable Act allows broadcasters to negotiate compensation from local cable operators in return for providing them with permission to retransmit their broadcast signals.[1] This provides broadcasters with a second revenue stream in addition to the revenue they earn from selling advertising. Congress believed

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[1] Cable Television Consumer Protection and Competition Act of 1992, Pub. L. No. 102-385, 106 Stat. 1460. *See also* 47 C.F.R. 76.64. In 1999, Congress enacted the Satellite Home Viewer Improvement Act, Pub. L. No. 106-113, 114 Stat. 1501, which allows DBS companies to offer local broadcast channels to their subscribers and allows broadcasters to negotiate compensation for providing them with retransmission consent. *See also* Satellite Home Viewer Extension Reauthorization Act ("SHVERA"), Pub. L. No. 108-447, 118 Stat. 2809 (2004).

that the potential social benefit of providing broadcasters with an extra revenue stream was that it might help preserve the viability and vigor of the broadcast industry and therefore result in a higher quality of broadcast programming. The potential social cost of this policy was of course that the cost of providing broadcasters with an extra revenue stream would be ultimately passed through to cable subscribers. At the time it passed the Cable Act, Congress apparently made the determination that the potential social benefits of this policy likely outweighed the potential social costs.[2]

Over a decade after retransmission consent was enacted, it is reasonable to review the evidence regarding the actual benefits and costs that retransmission consent policy has produced with an eye towards determining its impact on the marketplace and whether or not the policy needs to be changed. In particular, policymakers express concerns that (1) prices for the actual bundle of programs received by subscribers are too high and (2) subscribers may be forced to buy packages of programming that include programming that they have very little interest in, but for which they are nonetheless required to pay.[3] These concerns exist even though competition

[2] Congress was clearly aware that the social cost of retransmission consent regulations would be higher cable subscription prices and explicitly instructed the Commission to consider these costs when it implemented retransmission consent regulations. *See* 47 U.S.C. § 325(b)(3)(A) ("[t]he Commission shall consider in such proceeding the impact that the grant of retransmission consent by television stations may have on the rates for the basic service tier and shall ensure that the regulations prescribed under this section do not conflict with the Commission's obligation . . . to ensure that the rates for the basic service tier are reasonable."); House Conference Report 102-862, at 76 (1992) ("In the proceeding implementing retransmission consent, the conferees direct the Commission to consider the impact that the grant of retransmission consent by television stations may have on the rates for the basic service tier and shall [sic] ensure that the regulations adopted under this section do not conflict with the Commission's obligations to ensure that rates for basic cable service are reasonable").

[3] *See, e.g.,* Letter from John McCain, Chairman, US Senate Committee on Commerce, Science, and Transportation, to Michael Powell, Chairman, FCC, May 19, 2004. ("As you know, the Senate Committee on Commerce, Science, and Transportation has closely examined the issue of escalating cable rates in recent hearings. Cable rates have increased more than 50% since 1996 -

in the MVPD marketplace is quite strong and growing stronger. Since 1992, there has been tremendous growth in the number of program networks, direct broadcast satellite ("DBS") has penetrated the market with great success so that DBS companies have the second and fourth largest share of MVPD subscribers, the Internet and local telephone companies are finally making real progress into the video market, and there is widespread evidence that consumers value the services they receive. I will explain why an economic analysis of the available evidence suggests that retransmission consent authority as exercised by the network broadcasters is a significant cause of the problem.

The four major broadcast networks (ABC, NBC, CBS and Fox, the "the Big Four" or "the networks") negotiate retransmission consent agreements on behalf of all of their owned and operated ("O&O") stations.[4] The networks bundle their retransmission consent negotiations together with negotiations over license fees for cable channels that they also produce. They have used the threat that they might withdraw retransmission consent to force multi-channel video programming providers ("MVPDs") to (1) pay higher prices for programming that the operators

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almost three times the rate of inflation. These hearings have reinforced my concern that consumers lack options that would help them control the rising cost of cable and satellite television. When it comes to purchasing cable channels beyond the basic tier today, consumers have virtually no choice but to pay for a large package of expanded basic channels even if they watch only a couple of the channels.")

[4] In this paper, I will focus on retransmission consent agreements negotiated by the four major networks on behalf of their O&O stations. These are the agreements that have received the most public scrutiny and for which there is the most information available. O&O stations reach a significant share of nationwide viewers; local stations in the largest and most profitable urban areas all tend to be O&O stations. The share of viewers reached by O&O stations for each of the four major networks is: CBS 44.78% (FCC figure = 38.92%); Fox 44.55% (FCC figure = 37.92%); NBC 38.30% (FCC figure = 33.56%); and ABC 23.72% (FCC figure = 23.72%). *See Top 25 Station Groups*, Broadcasting and Cable, April 19, 2004. The FCC figure incorporates a 50% discount for UHF stations. To the extent that non-O&O's are able to negotiate significant compensation from retransmission consent agreements, this would further increase the social cost of these regulations.

might have purchased in any event, and (2) purchase additional programming that they might otherwise not have purchased.

The networks have generally chosen to tie retransmission consent to the carriage of relatively new channels that they are attempting to introduce and develop a market for rather than to carriage of mature already-popular channels. Programmers not affiliated with the four major broadcasters generally have difficulty arranging carriage for their new networks and often are forced to charge no license fee and perhaps even to make cash payments to MVPDs in return for carriage. In contrast, programmers affiliated with one of the networks are generally able to charge positive license fees even when new channels are first introduced and still achieve wide initial distribution. The costs to MVPDs of paying higher license fees than they would otherwise be willing to pay and of buying programs that they would otherwise be unwilling to buy are largely passed on to subscribers in the form of higher subscription prices. Consumers also are harmed because these tie-ins reduce competition in the market for network programming and distort the selection of programs that is available to MVPD subscribers.

The social costs of retransmission consent may be somewhat hidden from view since they are not paid for as a separate, easily identifiable item, but are instead bundled together with payments for other program networks produced by the Big Four. However, consumers pay these costs just as surely whether or not they are identified as a separate line item. Furthermore, the available evidence suggests that the Big Four possess significant market power and that they are therefore able to extract significant compensation from MVPDs in return for providing them with retransmission consent. For example, in comments to the Commission, Disney has submitted expert reports that argue that a license fee of between $2.00 and $2.09 per subscriber per month would be a reasonable price for Disney to charge for retransmission consent for ABC if it were to charge a stand alone price. If Disney and the other major networks are each able to extract even a fraction of this amount from MVPDs, this would represent a very significant cost to MVPD subscribers.

While my main focus in this paper is to explain why an economic analysis of the available evidence suggests that retransmission consent regulations impose a significant social cost, I also briefly consider the issue of social benefits of the policy. Very little evidence of any sort has been presented suggesting that broadcasters have used the extra revenue stream provided to them by retransmission consent to invest in higher quality broadcast programming. Furthermore, simple economic theory does not necessarily predict that broadcasters would have the incentive to invest any of the additional revenue they receive due to retransmission consent policy in improving the quality of their broadcast programming.

Given that retransmission consent policy appears to create significant social costs and given that the social benefits of this policy are not readily apparent, I conclude that policymakers should attempt to more carefully investigate whether or not there are any social benefits to this policy with an eye towards changing the policy unless evidence can be found that significant social benefits exist that outweigh the social costs.

The paper is organized as follows. In Section I, I describe relevant developments that have occurred in the television industry since retransmission consent was enacted in 1992. In Section II, I explain the basis for my conclusion that the four major broadcast networks have significant market power and are thus able to negotiate significant compensation from MVPDs in return for providing them with retransmission consent. In Section III, I provide evidence that broadcasters have used the threat of withdrawing retransmission consent to force MVPDs to pay higher prices for cable programming than they would otherwise be willing to pay and/or to purchase and pay for cable network programming that they would otherwise be unwilling to purchase. I also explain from an economic perspective why a broadcaster with market power over his broadcast signal might choose to exercise this market power by bundling the signal together with non-broadcast network programming and charging a higher price for the bundle instead of directly charging a stand-alone cash price for retransmission consent. In Section IV, I explain why consumers are harmed by this exercise of market power. In Section V, I consider the potential social benefits of retransmission consent policy and observe that these benefits remain largely unproven. Finally, section VI draws a brief conclusion.

I. DEVELOPMENTS IN THE CABLE AND TELEVISION INDUSTRY SINCE THE PASSAGE OF RETRANSMISSION CONSENT REGULATIONS IN 1992

In this section, I document and explain the rise to dominance of the Big Four in the non-broadcast network program industry. I also briefly review some of the evidence that cable subscription rates have been increasing rapidly and that increases in programming costs have been a significant factor driving these increases.

A. The Rise of Broadcaster-owned MVPD Networks

The four major broadcast networks are now collectively the predominant suppliers of satellite-delivered networks. This represents a dramatic shift from a decade ago, when cable MSOs were the predominant suppliers of such network programming. Tables 1 and 2 below show the ownership shares of different firms in the satellite-delivered network programming industry for 1993 and 2004.

Table 1[5]
Ownership of National Basic Program Networks, 1993

Broadcast Networks:	Share of Ownership:
ABC	14.6%
CBS	0.0%
Fox	0.0%
NBC	3.6%
Total	**18.2%**
Cable MSOs or Their Affiliates:	**Share of Ownership:**
Cablevision	0.6%
Comcast	0.1%
Cox	1.3%
Liberty Media	2.1%
TCI	2.4%
Time Warner	1.4%
Turner	31.8%
Viacom	13.8%
United Cable	0.1%
Total	**53.6%**
Others:	**Share of Ownership:**
Total	**28.2%**
ALL OWNERS	**100%**

[5] *Source*: Kagan World Media, *Economics of Basic Cable Networks 1993* (*"Kagan (1993)"*). *Kagan (1993)* provides the net revenue and ownership data for each basic cable network for 1993. Calculation of the ownership shares of various companies in the basic cable network industry is then performed as follows. If some company "A" owns 50% of a particular basic cable network N and the net revenue for the basic cable network is $50 million then Company A is attributed with $25 million in net revenue because of its ownership of network N. The total attributable net revenue for Company A is calculated by summing its attributable revenue across all basic networks. The ownership share of company A in the basic cable network industry is then company A's attributable net revenue calculated as a percentage of the total net revenue for the entire industry.

Table 2[6]
Ownership of National Basic Program Networks, 2004

Broadcast Networks:	**Share of Ownership:**
ABC	20.9%
CBS	17.7%
Fox	8.1%
NBC	9.8%
Total	**56.5%**
Cable MSOs or Their Affiliates:	**Share of Ownership:**
Time Warner	16.1%
Cablevision	4.5%
Comcast	2.1%
Cox	1.6%
Newhouse	1.6%
Total	**25.9%**
Others:	**Share of Ownership:**
Liberty Media	4.3%
Others	13.3%
Total	**17.6%**
ALL OWNERS	**100%**

[6] *Source*: Kagan World Media, *Economics of Basic Cable Networks 2005* ("*Kagan (2005)*"). *Note: Kagan (2005)* provides the net revenue and ownership data for each basic cable network for 2004. Calculation of the ownership shares of various companies in the basic cable network industry is then performed as described in the note to Table 1 above.

Table 3 summarizes the nature of the changes that have occurred in the ownership structure of the non-broadcast network program industry between 1993 and 2004:

Table 3
Ownership Shares of National Basic Networks, 1993 to 2004[7]

Type of Owner	Share of Networks	
	1993	2004
Major Broadcast Networks	18.2%	56.5%
Cable MSOs	53.6%	25.9%
Other Types of Owners	28.2%	17.6%

As is evident, cable MSOs or their affiliates were the major owners of program networks in 1993. While the major broadcast networks owned some non-broadcast networks, their ownership share was less significant. However, by 2004 the relative positions of these two groups had been reversed.

Tables 4 and 5 show the identity and market share of the top five providers of satellite-delivered network programming in 1993 and 2004:

Table 4
Market Shares of Top Five Providers of MVPD Network Programming in 1993[8]

Owner	Type of Owner	Share
Turner	Vertically integrated with cable MSOs	31.8
ABC	Major Broadcast Network	14.6
Viacom	Vertically integrated with cable MSOs	13.8
Hearst	Publisher and Broadcast Group	5.9
Paramount	Studio and Broadcast Group	5.0
Total		**71.1**

[7] Tables 1 and 2 above.

[8] *Source: Kagan (1993)*. Shares are calculated as explained in the note to Table 1.

Table 5
Market Shares of Top Five Providers of MVPD Network Programming in 2004[9]

Owner	Type of Owner	Share
ABC	Major Broadcast Network	20.9
CBS	Major Broadcast Network	17.7
Time Warner	Cable MSO	16.1
NBC	Major Broadcast Network	9.8
Fox	Major Broadcast Network	8.1
Total		**72.6**

As set forth above, in 1993 only one of the top five providers was a major broadcast network; two were vertically integrated with cable MSOs and two owned broadcast groups. In 2004, four of the top five firms were major broadcast networks; the other was a cable MSO.[10] This data once again reflects the rise to dominance of the major broadcast networks in the MVPD programming industry over the past decade.

[9] *Source: Kagan (2005)*. Shares are calculated as explained in the note to Table 1.

[10] The MSO, Time Warner, includes the Turner networks and, as such, its share has declined over the last decade.

Table 6 provides a list of the main MVPD networks affiliated with each of the Big Four.

Table 6
MVPD Networks Affiliated with the Big Four[11]

News Corp. (Fox)	Viacom (CBS)	Disney (ABC)
Fox Movie Channel	BET	A&E (37.5%)
Fox News	BET on Jazz	ABC Family
Fox Sports World	CMT	Biography (37.5%)
Fuel	Comedy Central	History (37.5%)
FX	Flix	History International (37.5%)
National Geographic (67%)	MTV	Disney
Speed	MTV Espanol	E (39.5%)
	MTV Hits	ESPN (80%)
General Electric (NBC)	MTV Jams	ESPN Classic (80%)
A&E (25%)	MTV2	ESPN News (80%)
Biography (25%)	Nickelodeon	ESPN2 (80%)
Bravo	Nick Gas	Lifetime (50%)
CNBC	Nick Too	Lifetime Movie Network (50%)
History (25%)	Nicktoons	Lifetime Real Women (50%)
History International (25%)	Noggin	Style (39.5%)
MSNBC	Showtime	Soapnet
Sci-Fi	Spike	Toon Disney
Shop NBC	Sundance (30%)	
Sundance (50%)	TMC	
Trio	TV Land	
USA	VH1	
	VH1 Classic	
	VH1 Country	
	VH1 Mega Hits	
	VH1 Soul	

The expansion of the Big Four into the MVPD programming industry has, in fact, been large enough to more than offset the declines in broadcast viewership that have occurred over this period. Table 7 shows that, while the ratings of the broadcast programming produced by the Big Four have declined since 1997, the ratings of ALL the programming produced by the big four (i.e., broadcast networks plus MVPD networks) have actually increased.

[11] *Kagan (2005)* at 60, 79.

Table 7
Ratings of All Programming Produced by the Big Four, 1997-2003[12]

	1997 Prime Time Rating	2003 Prime Time Rating	% Change
ABC Network	9.3	6.7	-27.96
ABC Video Channels	2.0	5.0	144.8%
CBS Network	9.4	8.3	-11.70%
CBS Video Channels	0.0	6.3	n/a
NBC Network	10.7	7.7	-28.04%
NBC Video Channels	0.5	3.1	522.08%
Fox Network	6.7	5.9	-11.94%
Fox Video Channels	.3	2.1	607.87%
Total	**38.9**	**45.1**	**15.94%**

Thus, the networks have essentially *grown* their share viewership by migrating from the broadcast to the cable platform.

B. The Demise of Restrictions on Content Ownership and the Passage of Retransmission Consent Regulations Both Contributed to the Rise to Dominance of Broadcaster-Owned Program Networks

Beginning in the 1960's, the government started to curb the major broadcast networks' ownership of in-house programming, largely to address the concern that the networks would "take over" programming and use their control to eliminate competition in downstream distribution. As a result of antitrust litigation by the Department of Justice[13] and regulation by

[12] *Kagan (2005)* at 32, 44-45, 60; Cable Television Advertising Bureau. Ratings are weighted by ownership percentage in the network. Broadcast network ratings are from the first quarter of the year listed.

[13] The Department of Justice sued the major networks to limit their participation in production of the programming they broadcast. *See, e.g., United States v. Nat'l Broad. Co. Inc.,* 449 F.Supp. 1127 (C.D. Cal. 1978); *United States v. Am. Broad. Cos., Inc.,* 1980 WL 2013 (C.D. Cal.), 1981-1 Trade Cas. (CCH) ¶ 64, 150 (1980). The consent decrees ending the litigation required that the networks: (1) acquire only the right of first-run exhibition, (2) be prohibited from acquiring financial interests in a program produced by an outside source which would earn revenues for the network outside of the network run of the program, and (3) be prohibited from acquiring any domestic syndication rights. *Id.*

the FCC (the so-called fin/syn rules),[14] the major broadcast networks were eventually prohibited from producing or having a financial stake in most of the entertainment series they broadcast and from participating in the profits from syndicating re-runs of these shows.[15] However, in the early 1990's the networks fought successfully to reverse the FCC rules; meanwhile the antitrust consent decrees expired.[16] By 1995 the networks were no longer prohibited from producing their own programming and the result was a transformation of the television programming industry. Today the major networks are each vertically integrated with content assets and produce a significant amount of their own programming.

Table 8
Change in Big Four – Studio Affiliations[17]

Major Broadcast Network	Studio Affiliation 1992	Studio Affiliation Today
ABC	None	Walt Disney Studios Buena Vista Television Touchstone Pictures Hollywood Pictures Miramax Films Dimension Films
NBC	None	Universal Studios NBC Studios
CBS	None	Paramount Pictures Paramount Television King World Television CBS Enterprises

[14] The fin/syn rules were adopted in 1970 to "limit network control over television programming and thereby foster diversity of programming . . . ." *See In the Matter of Review of the Syndication and Financial Interest Rules, Sections 73.659-73.663 of the Commission's Rules,* 10 FCC Rcd 12165 (1995). The rules restricted the ability of ABC, NBC, and CBS to own and syndicate television programming.

[15] For more background, *see generally* Ken Auletta, THREE BLIND MICE 30-33, 76-77 (1991).

[16] *See generally Schurz Communications, Inc. v. FCC*, 982 F.2d 1043 (7th Cir. 1992).

[17] Hoovers Online, www.corporate.disney.go.com

Table 8
Change in Big Four – Studio Affiliations[17]

Major Broadcast Network	Studio Affiliation 1992	Studio Affiliation Today
Fox	20th Century Fox	20th Century Fox Fox Searchlight Fox Television

The proliferation of broadcast-owned MVPD networks during the last twelve years reflects in some measure the major broadcast networks' new incentives to invest in content production in the aftermath of the repeal of the fin/syn regulations and the expiration of the related consent decrees. This is because there are significant "economies of scope" for the networks between producing programming for their own use and producing programming that can be shown on MVPD networks. Once the networks were acquiring and/or producing significant amounts of content for use on their broadcast outlets, they found that they could use substantial amounts of in-house content that already existed and produce additional content at a relatively low incremental cost for distribution on affiliated MVPD networks.[18] In many cases,

[18] *See, e.g.*, "Fox's New Web Is A Special FX," *Variety*, September 1, 1993 (FX "will rely heavily on Fox's film and TV library material .... The basic channel provid[es] the studio an outlet for its product similar to Paramount and USA's ownership of the USA cable network"); "CBS Surrender May End Retransmission War," *Television Digest*, August 30, 1993 ("New [CBS] cable network would make extensive use of film and reports already being shot, but often not used, for CBS's existing news programs. . . .' They have a lot of footage that goes onto the cutting room floor. If they can recycle it, it's good for them'"); "Fox Weaves Cable Web With TCI," *Daily Variety*, May 13, 1993, ("Murdoch said Fox will spend 'in excess of $100 million in the first year' for programming on the new network .... 'We'll use movies from our library,' he added, and off-network series that Fox's Twentieth TV division produces for ABC, CBS, NBC and Fox. If Fox had run its own cable network three years ago, Murdoch said, it would probably not have sold reruns of 'L.A. Law to Lifetime'"). *See also* "CBS Ponders Cable Formats; In Retreat From Pay Or Else, Net Likely To Basic-Service Retrans Trade," *Hollywood Reporter*, August 27, 1993 (reporting CBS' decision to seek retransmission consent compensation in the form cable carriage for a new news and information cable channel, and noting that "a CBS News cable outlet would also provide CBS with a virtually cost-free revenue stream for repeat broadcasts of its highly rated magazine shows, while also giving it a much-

this gave them a competitive advantage over other rivals and contributed to their rise to dominance in the MVPD network programming industry.

While the demise of restrictions on content ownership certainly was a major factor explaining the rise to dominance of the Big Four in the MVPD network programming industry, it cannot be the sole explanation. This is because the restrictions on content ownership only applied to the original "Big Three" – CBS, ABC, and NBC - and in, particular, did NOT apply to Fox. As documented above, all FOUR of the major networks transformed themselves to become major owners of MVPD network programming during the last decade. In fact, as will be detailed further below, many industry observers attribute Fox with taking a leadership role in this transformation with its launching of the FX network. Since the restrictions on owning content never applied to Fox in the first place, the repeal of these restrictions should not have been expected to create either the incentive or opportunity for Fox to expand into the MVPD network programming industry.

An examination of the historical record dating from this time period suggests that the enactment of retransmission consent regulations played a role in Fox's rise in the MVPD network programming industry. In particular, it was widely reported at the time that the networks and cable MSOs had reached a bargaining impasse after the passage of retransmission consent regulations in 1992 and the Fox led the way to resolving the impasse by creating a new network, FX, and agreeing to provide retransmission consent in return for MSOs' agreement to

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needed promotional platform for the network news organization"); "ABC Reusing Toon Model," *Electronic Media*, April 12, 1999 (noting that Disney viewed retransmission consent as a "valuable bargaining chip with cable operators," regarding carriage of Disney-owned cable channel, SoapNet, whose "core" programming are "four ABC-owned soap operas").

accept and pay for FX.[19] Two of the other major networks then quickly followed suit by launching their own new cable networks. In comments filed with the FCC in the *A La Carte Inquiry*,[20] Disney itself describes the initial bargaining standoff that occurred between broadcasters and cable systems when retransmission consent regulations were first introduced and explains that the standoff was resolved by bundling:

> This standoff was resolved when three of the then four major broadcast networks agreed to proposals to grant Retransmission Consent for network-owned stations in return for cable carriage of, and payment for, new network-owned cable channels. In return for granting broadcast Retransmission Consent, Fox was able to launch the cable network FX, ABC was able to launch ESPN2 and NBC was able to launch 'America's Talking' (which later became MSNBC).[21]

In summary, the repeal of fin\syn regulations and the expirations of related consent decrees cannot explain Fox's dramatic entry into the cable network programming industry. This is because the regulations and consent decrees did not apply to it in the first place. I believe that the evidence strongly suggests that the passage of retransmission consent regulations was a major factor explaining the launch of FX. Since the passage of retransmission consent regulations created essentially the same set of economic incentives for all four of the networks, and since there is evidence that retransmission consent regulations likely played a significant role in explaining Fox's entry and prominent position in the MVPD network programming industry, I

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[19] *See, e.g.*, "Fox's New Web Is A Special FX," *Variety*, September 1, 1993 ("Fox created the basic channel as its solution to negotiations over retransmission consent, in the process providing the studio an outlet for its product similar to Paramount and USA's ownership of the USA cable network.")

[20] *In the Matter of A La Carte and Themed Tier Programming and Pricing Options for Programming Distribution on Cable Television and Direct Broadcast Satellite Systems*, MB Docket No. 04-207 (May 25, 2004) ("*A La Carte Inquiry*").

[21] Comments of The Walt Disney Company, MB Docket No. 04-207, at 41-42 (Jul. 15, 2004).

conclude that these regulations likely also played a similar role in explaining the entry and rise to dominance in cable programming of the other three networks.

Of course, the entry of the other three networks into the MVPD network programming industry would not have been possible without the demise of restrictions on content ownership by the three networks. Furthermore, it seems likely to me that, once they owned studios of their own, the networks would have entered the MVPD network programming industry to some extent regardless of whether or not retransmission consent had been enacted. But the facts that: (1) these content restrictions never applied to Fox, (2) Fox's dramatic transformation into a dominant player in the cable network programming industry did not occur until passage of retransmission consent regulations and (3) Fox explicitly negotiated agreements with MSOs in which they agreed to accept FX in return for receiving retransmission consent, all seem to suggest that the enactment of retransmission consent regulations also played a significant role in causing the rise to dominance of the Big Four in the cable network programming industry.

C. Increases in Cable Subscription Prices Have Been Fueled by Increases in Programming Costs

Cable subscription prices have been rising at a very fast rate since passage of the Telecommunications Act in 1996 and this rapid rate of increase has been a serious source of concern to policymakers. In a recent report, the GAO summarizes the situation as follows:

> FCC data indicate that the average monthly rate subscribers are charged for the combined basic and expanded-basic tiers of service rose from \$26.06 in 1997 to \$36.47 in 2002 – a 40 percent increase over the 5 years. This rate of increase is much much greater than the general rate of inflation, as measured by the Consumer Price Index (CPI), which rose 12 percent over the same period.[22]

[22] *See* GAO, *Issues Related to Competition and Subscriber Rates in the Cable Television Industry,* GAO-04-8, at 20 (Oct. 2003) (*"GAO (2003)").*

The Commission recently released its *2004 Report on Cable Industry Prices*,[23] finding that the five-year annual increase was 7.5 percent and the five-year annual increase in the number of channels was 6.3 percent, for the period ending January 1, 2004.

It is well-recognized that cable operators' costs of purchasing programming have also been rising at a very rapid rate and that a substantial share of the price increases that consumers have experienced simply reflects a pass-through of these cost increases. According to the GAO, for example,

> [O]ne important factor contributing to higher cable rates is cable operators' increased costs to purchase programming from cable networks. . . On the basis of financial data supplied to us by 9 cable operators, we found that these operators' yearly programming expenses, on a per-subscriber basis, increased from $122 in 1999 to $180 in 2002 - a 48 percent increase. Using data from Kagan World Media, we found that the average fees cable operators must pay to purchases programming (referred to as license fees) increased by 34 percent from 1999 to 2002.[24]

In a study of my own, using FCC data,[25] I calculated that between 1999 and 2002 the price of expanded basic cable TV service increased by $7.06 per subscriber per month and that during this same time period the net cost[26] of expanded basic programming increased by $2.96 per subscriber per month. Therefore, based on this data, 42% of the increases in expanded basic cable TV prices over this period were necessary to cover the increased cost of programming.

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[23] *See In the Matter of Implementation of Section 3 of the Cable Television Consumer Protection and Competition Act of 1992, Statistical Report on Average Rates for Basic Service, Cable Programming Service, and Equipment*, FCC 05-12, MM Docket No. 92-266 (rel. Feb. 4, 2005).

[24] *See Kagan (2003)* at 21-22.

[25] *See* William P. Rogerson, *Correcting the Errors in the ESPN/CAP Analysis Study on Programming Cost Increases*, November 11, 2003 (study prepared for Cox Communications).

[26] The cost of program license fees is to some extent offset by income earned from advertising and the appropriate measure of the cost of license fees to use is license fees net of income earned from advertising.

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In summary, since the passage of retransmission consent, the Big Four broadcasters have grown to dominate the MVPD network programming industry. Subscription prices for cable TV have risen significantly over the past decade, and there is wide agreement that increases in programming costs have been an important factor fueling these price rises. I will now go on to explain why the passage of retransmission consent regulations likely played a major role in contributing to these increases in programming costs by allowing broadcasters to exercise their market power over their broadcast signals.

II. THE FOUR MAJOR BROADCAST NETWORKS HAVE MARKET POWER THAT HAS LIKELY INCREASED SINCE PASSAGE OF THE 1992 CABLE ACT

I believe that the signals of the four major broadcast networks are "must have" programming in the sense that the customers of MVPDs value this programming highly and do not perceive that there are good substitutes for it. This means that an MVPD that found itself unable to offer the one of the four major broadcast signals would lose subscribers to rival MVPDs and thus suffer a reduction in its profits. As a consequence, MVPDs place a high value on this programming, and the networks are able to negotiate significant compensation from MVPDs in return for providing them with permission to retransmit this programming.

I will begin by describing the two principal types of evidence that support the conclusion that the signals of the four broadcast networks are "must have" programming which create market power for their providers. Then I will note that both the Commission (in its review of the New Corp./ DirecTV merger) and Disney itself (in comments submitted to the Commission in the *A La Carte Inquiry*) have reviewed similar sorts of evidence and reached precisely the same conclusion. Finally, I will conclude by explaining why it is likely that competitive developments that have occurred in the MVPD market since passage of the Cable Act in 1992, have, somewhat paradoxically, had the effect of *increasing* the market power of the Big Four.

A. There Is Substantial Evidence That the Networks Have Market Power

There are two principal types of evidence that exist to support the conclusion that the signals of the four broadcast networks are "must have" programming that create market power for their providers. First, there is substantial evidence that cable subscribers have responded to the temporary withdrawal of broadcast signals from cable operators by switching to alternate MVPDs. Second, customer response to local-to-local offerings by DBS providers has confirmed that consumers highly value provision of local broadcast signals.

1. Customer Response to Temporary Withdrawals of Retransmission Consent from MPVDs Confirms That Broadcast Signals Are "Must Have" Programming

There have been a number of well-publicized incidents in the last few years where the signal of one of the major networks has been taken off an MVPD during retransmission consent negotiations. The evidence suggests that significant numbers of customers leave the MVPD that can no longer offer the local station, and, instead, switch to another MVPD that can. Furthermore, MVPDs that are still able to offer the local station typically heavily advertise this fact in an attempt to steal customers away from the affected MVPD. The fact that an MVPD will lose a substantial number of customers if it is unable to retransmit the signal of broadcasters is of course the underlying reason why broadcasters are able to demand significant compensation in return for retransmission consent.

In a recent case from the Washington, D.C. area, News Corp. withheld the signal of Fox station WTTG-TV during a retransmission consent negotiation.[27] The dispute arose near the

[27] *See* Comments of Cox Enterprises, Inc., MB Docket No. 02-277, at 45 (Jan. 2, 2003).

beginning of the NFL playoffs.[28] The Washington Times reported that during the course of negotiations, satellite providers "profited[ed] from the disruption of service, aggressively marketing themselves to consumers as an alternative to Cox."[29] Eventually, Cox Communications agreed to News Corp.'s demands and the signal was restored.

A retransmission consent dispute between Disney and Time Warner resulted in the ABC network being withheld from 3.5 million Time Warner subscribers for 39 hours on May 1 and 2, 2000. The New York Post reported that "Time Warner's spat with ABC could end up costing the cable giant $150 million worth of lost subscribers."[30] The Commission carefully investigated the extent to which subscribers switched from Time Warner to DBS providers in response to this incident in the Houston area using confidential data supplied by various parties. While it did not release its estimate of the number of consumers that switched, it concluded, based on its analysis of subscriber shifts in this case, that the response was "representative of the shifts of customers that could occur during a long-simmering dispute over retransmission consent"[31] and that in such disputes "the subscriber shifts required for temporary foreclosure to be profitable are likely to be realized."[32]

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[28] *See* Linda Moss, "Some Subs Who Lost Fox Get Refunds from Cox," *Multichannel News*, January 17, 2002, at 3.

[29] *See* Kristina Stefanova, "Satellite Soaring; Fox-Cox Flap Also Sells Antennas," The Washington Times, January 4, 2000, at B8.

[30] Lisa Brownlee, *Paying the Price - ABC Re-DirecTVs $150M From Time Warner,* May 18, 2000, 037.

[31] *In the Matter of General Motors Corporation and Hughes Electronics Corporation, Transferors, and The News Corporation, Transferee, For Authority to Transfer Control, Memorandum Opinion and Order*, 19 FCC Rcd 473, 568 ¶ 208 (2004) ("*News Corp./DirecTV Merger Order*").

[32] *Id.* at ¶ 206.

The most recent incident involves Viacom and Echostar. During negotiations over retransmission consent, CBS became unavailable to 1.6 million Echostar subscribers for two days in March 2004. It was widely reported in the press that Echostar backed down in its demands almost immediately because it feared losing customers to competing MVPDs that still carried Viacom programming. For example, while the dispute was still ongoing, the New York Times reported that "Most media analysts said that Echostar had more to risk in the fight than Viacom because rival cable systems and satellite companies would begin vying for disgruntled EchoStar customers."[33] It quoted Craig Moffet, an analyst at Stanford C. Bertstein & Company as stating that "the cost to EchoStar in potential subscriber losses would be astronomical."[34] On the same day, the Wall Street Journal noted that "Some cable companies have launched advertising campaigns to exploit EchoStar's loss of CBS and Viacom's cable networks."[35] A day later, when the dispute was settled, the Wall Street Journal reported that "The pact appears to be a retreat by Echostar Chairman and Chief Executive Charles Ergen, who acknowledged accepting roughly the terms that were on the table at the height of the impasse."[36]

2. Customer Response to Local-to-Local Offerings of DBS Providers Confirms That Broadcast Signals Are "Must Have" Programming

DirecTV and Echostar claim that their ability to attract customers away from cable increased significantly when the passage of SHVIA allowed them to begin offering local broadcast signals; this provides more evidence that local signals are "must have" programming.

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[33] Bill Carter & Geraldine Fabrikant, "Accord Said to be Near in Viacom-EchoStar Dispute," New York Times, March 11, 2004, at C1.

[34] *Id.*

[35] Joe Flint, "They Killed Kenny! And Spongebob!; Viacom Puts Echostar Feud On Prime Time to Raise Pressure in Contract Talks," Wall Street Journal, March 11, 2004, at B3.

[36] Andy Pasztor and Joe Flint, "Viacom and Echostar Reach Accord on New Contract Terms,"

In filings with the Commission, EchoStar reports that the addition of local channels has made DBS more competitive with incumbent cable providers and has led to an increase in DBS subscribership and a restraint on cable prices,[37] and DirecTV reports that its overall subscriber levels have increased by 20 percent due to the provisioning of local broadcast channel service.[38] The Commission itself has recognized that the offering of local channels has allowed DBS providers to make significant gains in the MVPD market:

> DBS providers have made significant progress as competitors to cable, capturing 18 percent of MVPD subscribers, due in part to authority granted by SHVIA to DBS operators to distribute local broadcast television stations in their local markets. Indeed, we believe that the marked growth of DBS since the enactment of SHVIA provides an informative example of the impact on competition in the distribution of video programming when marketplace participants gain access to valuable programming to which they were previously denied.[39]

The GAO has conducted its own analysis of subscription data and concluded that "the provision of local broadcast channels by DBS companies is associated with significantly higher DBS penetration rates."[40]

Wall Street Journal, March 12, 2004, at B5.

[37] *See In the Matter of Annual Assessment of the Status of Competition in the Market for Delivery of Video Programming, Ninth Annual Report*, 17 FCC Rcd 26901, 26931-32 ¶ 61 (2002).

[38] *See In the Matter of Annual Assessment of the Status of Competition in the Market for Delivery of Video Programming, Eighth Annual Report*, 17 FCC Rcd 1244, 1273-74 ¶ 59 (2002).

[39] *In the Matter of Implementation of the Cable Television Consumer Protection And Competition Act of 1992, Development of Competition and Diversity in Video Programming Distribution: Section 628(c)(5) of the Communications Act, and Sunset of Exclusive Contract Provision, Report and Order,* 17 FCC Rcd 12124, 12143 ¶ 44 (2003).

[40] GAO, *Issues in Providing Cable and Satellite Television Services*, GAO-03-130, October 2002, at 3.

B. The Commission Has Concluded, Based on Its Own Evaluation of the Evidence, That News Corp. Possesses Market Power and this Reasoning Applies Equally Well to the other Three Networks

In the Commission's review of the proposed merger between News Corp. and DirecTV, a central issue was whether or not News Corp. possessed market power because of its ability to deny retransmission consent of the Fox network to MVPDs. The Commission had access to a comprehensive public record, as well as to confidential data provided by MVPDs and News Corp., regarding retransmission consent negotiations and the MVPD marketplace. The Commission devoted an entire section of its report to the issue of retransmission consent. After providing some background information and describing the positions of the parties, the Commission stated its conclusions in a subsection entitled "Discussion." The first paragraph of this subsection states:

> We find that News Corp. *currently possesses* [emphasis added] significant market power in the DMAs in which it has the ability to negotiate retransmission consent agreements on behalf of local broadcast television stations. Local broadcast station programming is highly valued by consumers, and entry into the broadcast station market is difficult.[41]

The second paragraph states:

> At the outset, we agree with commenters who contend that carriage of local television broadcast station signals is critical to MVPD offerings. Congress has repeatedly recognized the importance of carriage of local television broadcast signals to MVPDs - most recently when it enacted SHVIA, which permitted DBS operators to carry local television broadcast signals so that they could better compete with cable operators. As we recently found in our annual video competition report, DBS penetration has increased more rapidly in markets where local-into-local service is available. We also agree with commenters who contend that News Corp. *possesses market power* [emphasis added] in the broadcast station segment of the video programming market. We base this finding, in part, on the fact that the signals of local television broadcast stations are without close substitutes.[42]

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[41] *News Corp./DirecTV Merger Order* at ¶201.

[42] *Id.* at ¶ 202.

All of the Commission's reasoning and conclusions apply equally well to the other three major networks.

I expect that critics of my paper may try to argue that the Commission should disregard all of the conclusions that it arrived at in its analysis of the News Corp./DirecTV merger because the Commission was only ultimately concerned in its review of this merger with the incremental effects of the merger. Such an argument would not be correct. In its report, the Commission explicitly states that it reaches two different conclusions. The first conclusion is that News Corp. has significant market power because of retransmission consent. The second conclusion, the issue before the Commission raised by the transaction, is that News Corp.'s acquisition of a controlling interest in DirecTV will increase this market power. I have provided the first two paragraphs of this subsection of the Commission order, above, that describe the Commission's conclusion that News Corp. has significant market power due to retransmission consent. Neither of these paragraphs deal with the incremental effect of the merger. Rather, they both unequivocally state the Commission's conclusion that News Corp. has market power even without the vertical merger. It is not until the third paragraph of the discussion section that the Commission turns to the issue of the incremental effect of the transaction. I will provide the text of this third paragraph below. Note that the Commission explicitly describes this paragraph as offering a "further" conclusion:

> We *further* [emphasis added] find that News Corp.'s existing control of MVPDs' access to a large number of local broadcast stations airing highly popular Fox network programming, when combined with ownership of a nationwide DBS platform, will likely increase News Corp.'s incentive and ability engage in temporary foreclosure strategies aimed at increasing its programming fees thereby

> having the effect of raising rival MVPD's costs by lowering the costs to News Corp. of engaging in such behavior.[43]

Therefore, while the Commission's ultimate focus in its review of the News Corp./DirecTV merger was to assess the incremental effect the transaction, it inescapably needed to consider the underlying more general issue of whether or not retransmission consent creates market power for broadcasters and it explicitly concluded that it does. While the Commission's specific conclusion that the New Corp./DirecTV merger would have harmful effects is not directly relevant to evaluating retransmission consent regulations, the Commission's more general conclusion that broadcasters have market power with respect to their broadcast signals most certainly is relevant. Specifically, the Commission's conclusion that broadcasters have market power over their broadcast signals necessarily implies that retransmission consent allows broadcasters to negotiate significant compensation from MVPDs. To the extent that MVPDs pass these costs through to subscribers, this means that retransmission consent regulations create a significant social cost. Of course the Commission did not attempt to specifically quantify the magnitude of this social cost in its analysis of the News Corp./DirecTV merger. Furthermore, the Commission might still determine that the net effect of retransmission consent regulations was positive if it determined that the policy created benefits that outweighed the costs. However, I think it is fair to say that the Commission's own conclusions in its analysis of the News Corp./DirecTV merger imply that retransmission consent policy likely creates a significant social cost.

The issue of retransmission consent arose in the Commission's recent *A La Carte Inquiry.* In its report to Congress on its findings, there is a paragraph that begins as follows:

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[43] *Id.* at ¶ 203.

> Certain parties have argued that the Commission's analysis of the [News Corp./DirecTV merger] bears some relevance on the present discussion. [footnote omitted] This represents a misunderstanding of the nature of the Commission's transactions review process as well as the specifics of the transaction between News Corp. and Hughes Electronics. The transaction review process at the Commission is directed at examining *changes* in the competitive landscape that are a direct result of the transaction at issue.[44]

I suppose that it would be possible to interpret this paragraph as meaning that the Commission believes that all of the factual determinations that it made on all possible subjects in its order on the News Corp./DirecTV merger are completely irrelevant to retransmission consent. I do not believe this would be a correct interpretation. I believe the correct interpretation is that the Commission is stating that its specific conclusion that the vertical merger between News Corp. and DirecTV would create competitive harms is not directly relevant to retransmission consent. However, factual determinations it made about issues that are directly relevant to retransmission consent are not rendered irrelevant simply because they were stated in the order addressing the News Corp./DirecTV merger. In particular, the Commission's determination that News Corp. possesses market power with respect to its broadcast signal is most surely relevant for analyzing the social costs and benefits of retransmission consent.

C. Disney Has Submitted Expert Testimony to the Commission Claiming that the Fair Market Value of Retransmission Consent for ABC is Between $2.00 and $2.09 Per Month

The Walt Disney Company has submitted a study by Economists Inc. attached to its comments for the *A La Carte Inquiry* that claims to show that the fair market value of retransmission consent for ABC is between $2.00 and $2.09 per subscriber per month.[45] Disney

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[44] *See Report on the Package and Sale of Video Programming to the Public*, at 70 (rel. Nov. 18, 2004) ("*A La Carte Report*").

[45] *See* Michael G. Baumann & Kent W. Mikkelsen, "The Fair Market Value of Local Cable Retransmission Rights For Selected ABC Owned Stations," *Economists Inc.*, July 15, 2004

points out that, while it generally offers retransmission consent to MVPDs as part of a package that requires the MVPD to purchase specified cable network programming at specified prices, it also offers MVPDs the option to purchase unbundled retransmission rights for ABC for a license fee that generally varies between 70 and 80 cents per subscriber per month. Disney endorses the conclusion of the Economists. Inc. study that the fair market value of retransmission consent is actually between \$2.00 and \$2.09 and argues that this provides evidence that its retransmission consent charges are perfectly reasonable.

As I understand Disney's argument it is stating that (i) it hired Economists Inc. to directly measure the size of its market power (ii) Economists Inc. reported that Disney has enormous market power and (iii) Disney would like the Commission to give it credit for the fact it is apparently exercising some restraint and not taking full advantage of its market power. I will leave the third and last issue to the Commission. For the purposes of my report it is sufficient for me to note that Disney itself claims that it has enormous market power and has submitted and endorsed an economic study that claims to demonstrate this.[46]

D. The Emergence Of DBS As A Viable Competitor To Cable Has Increased The Market Power Of Broadcasters

Importantly, the emergence of DBS as a competitor to cable has also served to increase the amount of bargaining power held by the major networks and therefore has increased the

(submitted as attachment to Comments of The Walt Disney Company (Jul. 15, 2004)).

[46] Parenthetically, I should note that I do not necessarily endorse all of the methodologies that Disney's experts used and, at a minimum, it seems to me that there are some troublesome gaps in Disney's logic. Disney doesn't bother to explain why it charges between 70 and 80 cents if it could actually charge over \$2.00. Furthermore, although Disney does not provide any information in this regard, it may be that almost all of Disney's customers choose to purchase the bundled package rather than paying the stand-alone retransmission price. However, even if each broadcaster was able to extract a fraction of \$2.00 per subscriber per month from MVPDs, this would impose a significant cost on MVPD subscribers.

extent to which broadcast networks are able to use retransmission consent regulations to extract higher payments from MSOs. As I have discussed above, the bargaining power of a broadcast network is created by the threat to withhold its signal and the negative impact this will have on the MVPD. When there was a single MSO serving an area, customers of the MSO that considered leaving it only had the option of taking over-the-air service. To the extent this option was not attractive, this would reduce the amount of defections the MSO would experience and thus reduce the network's bargaining power.

Now that the cable MSO competes with two DBS providers, customers of the MSO also have the option of switching to one of the DBS providers. This means that the MSO will likely experience greater defections of customers if it is unable to offer a broadcast signal. This increases the bargaining power of the network. Thus broadcasters are in a very different bargaining position today than Congress understood them to be in 1992 when it originally gave broadcasters the right to bargain for compensation for retransmission consent.

E. The Continuing Fragmentation of the Viewing Audience for MVPD Networks May Reinforce The Market Power of Broadcasters

It is widely recognized in the media industry that broadcast networks are able to command a much higher cost per viewer (advertising rates are generally quoted in CPMs or cost per thousand viewers) than are MVPD networks because of broadcast networks' ability to deliver much larger audiences in one sitting than cable networks can. The Commission's Office of Plans and Policy sums up the situation as follows:

> [I]n general, cable advertisements do sell at a significant CPM discount to broadcast. A recent analysis of 2001-02 data . . . suggests that the cable 'discount' ranged from 30 to 60 percent, depending on the daypart and the demographic target of the cable network. Interestingly enough, the analysis showed that the cable discount is apparently slightly larger than it was four years back during the 1997-98 season.[47]

Broadcasting and Cable reports similar findings for the period 2001-02. It also provides data for 2004 and reports that the CPM gap between broadcast and cable rates continued to widen over this period.

> [T]hree years ago, general-entertainment cable networks like TNT, USA Network, and FX sold many of their prime time spots at a fat 54% CPM discount to broadcast fare. This season, that gap is even fatter: 66%. And in the demo that advertisers chase most, adults 18-49, cable's discount for shows like FX's *The Shield* widened from 54% to 60% today. Similarly, cable news networks were selling at a 44% discount to broadcast news shows. Now that's widened to 47%.[48]

Broadcasting and Cable's explanation for the fact that the gap is widening is that the increasing proliferation of MVPD channels has resulted in an even more fragmented MVPD audience than before and that this has therefore increased the relative attractiveness of the large audiences that broadcast networks can deliver.

> Cable, ironically, is a victim of its own success. As it steals audience from networks, advertisers have fewer opportunities to reach millions of broadcast viewers at once. That scarcity gives NBC, CBS, and the other established networks the leverage to jack up prices for their big-reach shows, those drawing 10 million - 20 million viewers.[49]

The Washington Post quotes John Rash, a media buyer with Campbell Mithun, an advertising and marketing firm as making the same point.

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[47] Jonathan Levy, Marcelino Ford-Levine & Anne Levine, "Broadcast Television: Survivor in a Sea of Competition," Office of Plans and Policy Working Paper 37, September 2002, at 24-25.

[48] John M. Higgins, "The Great Divide: Why is the CPM Gap Widening if Cable Keeps Grabbing Viewers From Broadcast?," *Broadcasting and Cable*, March 29, 2004.

[49] *Id.*

> In the law of unintended consequences, the more fragmented the media landscape becomes, the more integral network TV ironically becomes as the last bastion of national reach. Accordingly, they are able to defy gravity by procuring higher [prices] despite lower ratings.[50]

The fact that broadcast networks can command such significantly higher advertising rates than many MVPD networks, and that this advantage appears to be increasing, suggests that broadcast networks will be able to maintain and solidify their ability to acquire and deliver program content more suited to the mass audience than other video programming networks can -- and thereby maintain or increase their market power.

III. BROADCASTERS USE THEIR MARKET POWER IN RETRANSMISSION CONSENT NEGOTIATIONS TO OBTAIN HIGHER LICENSE FEES AND TO OBTAIN CARRIAGE OF NEW NETWORKS

A. Networks Use Carriage Of Affiliated Program Networks As Currency In Retransmission Consent Negotiations

There appears to be almost complete and unanimous agreement among industry participants and observers, including the broadcasters themselves, the press, industry analysts, and the Commission that broadcasters bundle retransmission consent together with other cable programming they produce and use this as a bargaining chip to negotiate some combination of higher license fees and increased carriage than they otherwise would have been able to negotiate. Broadcasters have generally chosen to tie retransmission consent to the carriage of relatively new channels that they are attempting to introduce and develop a market for rather than to carriage of mature already-popular channels. Programmers not affiliated with the four major broadcasters generally have difficulty arranging carriage for their new programs and often are required to charge no license fee and perhaps even make cash payments to MVPDs in return for receiving

[50] Frank Ahrens, "Peddling Prime Time," Washington Post, June 15, 2004, at E01.

carriage.[51] In contrast, programmers affiliated with one of the four major broadcasters are generally able to charge positive license fees *even when the channel is first introduced* and still achieve wide initial distribution. The costs to MVPDs of paying higher license fees than they would otherwise be willing to pay and of buying programs that they would otherwise be unwilling to buy are largely passed on to MVPD subscribers in the form of higher subscription prices. Consumers also are harmed to the extent that these tie-ins reduce competition in the market for network programming and distort the selection of programs that is available to MVPD subscribers.

This pattern was established with the first round of retransmission consent negotiations that occurred in 1992 immediately after passage of the Cable Act. As I have already described in section I of this paper, Fox led the way to led the way to resolving the original bargaining impasse that occurred after passage of retransmission consent regulations by creating a new network, FX, and agreeing to provide retransmission consent in return for MSOs' agreement to accept and pay for FX.[52] ABC and NBC then quickly followed suit by launching, respectively, ESPN2 and America's Talking (later to become MSNBC). The Commission itself has observed that the first round of retransmission consent negotiations set the pattern that was subsequently followed:

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[51] *See Kagan (2005)* at 8 ("[O]perators are increasingly looking to start-ups to provide marketing subsidies to pay for higher profile on digital platforms."); *Id.* at 21 (For a start-up network the typical pattern is "a loss of $100+ mil. prior to breakeven which doesn't come for five, six or sometimes seven years."); Kagan World Media, *Media Trends 2004*, December 2003, at 43 ("most [new networks] are now offered for two years free and then rates stagger in over a number of years.") ("*Kagan (2004)*").

[52] *See, e.g.*, "Fox's New Web Is A Special FX," *Variety*, September 1, 1993 ("Fox created the basic channel as its solution to negotiations over retransmission consent, in the process providing the studio an outlet for its product similar to Paramount and USA's ownership of the USA cable network.").

> In 1993, retransmission consent disputes between cable operators and television stations threatened the continued cable carriage of many local broadcast stations in Connecticut and elsewhere. [footnote omitted] This and other disputes were resolved when three of the then four major broadcast networks agreed to proposals to grant retransmission consent for network-owned stations in return for cable carriage of, and payment for, new network-owned cable channels. In the years to follow, in return for granting retransmission consent, many networks were able to successfully launch new cable networks through retransmission consent negotiations.[53]

FX brought Fox an additional $.25 per subscriber per month - as well as advertiser revenues - for a brand-new untested network.[54] Many questioned whether FX justified such a high license fee.[55] Of course the reason that the fee appeared to be higher than the value of FX would justify was because MSOs were actually paying for the right to retransmit the Fox network as part of their payment that was nominally for FX.

The American Cable Association, which represents over 1,000 of the smaller cable providers in the United States, has provided numerous specific examples of cases where retransmission consent has been tied to the requirement that their members carry new networks in a long series of filings it has made to the Commission.[56] In its most recent filing, it provides a

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[53] *See A La Carte Report* at 73.

[54] *See* Halonen, "Looking Back at Retransmission: Stations, Cable Operators Questioning Validity of Regulations 10 Years Later," *Electronic Media*, March 4, 2002 ("But before broadcast signals disappeared from cable screens nationwide, News Corp. chief Rupert Murdoch broke the impasse with a face-saving deal in which he swapped retransmission rights for Fox stations to TCI in exchange for the cable MSOs support of a new Fox cable channel, FX, along with a fee of 25 cents per subscriber.").

[55] *See* Dempsey, "Cablers, FX in Fee Battle," *Daily Variety*, June 10, 1998, at 22 ("'FX doesn't have that kind of market power,' said Jedd Palmer, senior VP of programming for Media One, the third largest cable operator in the U.S. Mike Eagan, one of the partners of Renaissance Media, another owner of cable systems said, 'FX will be hard-pressed to maintain the kinds of license fees that it's accustomed to.' The license fee of FX is $.28 a month a subscriber, which puts it at the mid- to high end of the scale for general-entertainment networks.").

[56] *See* Comments of the American Cable Association, CS Docket Nos. 98-120, 00-96, 00-2 (Jun. 8, 2001); American Cable Association, *Petition For Inquiry Into Retransmission Consent*

table listing program networks of each of the four broadcasters that ACA members report that they have been forced to carry because of retransmission consent negotiations. These are reported in Table 9, below.

Table 9
Program Networks Carried Because of Retransmission Consent Tie-Ins
As Reported by the ACA[57]

	ABC	NBC	CBS	Fox
CNBC		•		
Comedy Central			•	
Disney (on basic tier)	•			
ESPN Classic	•			
ESPN News	•			
ESPN2	•			
Fox Movies				•
Fox News				•
Fox Sports				•
Fuel				•
FX				•
Lifetime Movies	•			
Lifetime Real Women	•			
MSNBC		•		
MTV Espanol			•	
MTV Hits			•	
MTV2			•	
National Geographic				•
Nick Gas			•	
Nicktoons			•	
Noggin			•	

Practices (Oct. 1, 2002); American Cable Association, *ACA Petition For Inquiry into Retransmission Consent Practices: First Supplement*, (Dec. 9, 2002); Comments of the American Cable Association, MB Docket No. 04-207 (Jul. 12, 2004) ("*ACA A La Carte Comments*").

[57] *ACA A La Carte Comments* at 33.

Table 9
Program Networks Carried Because of Retransmission Consent Tie-Ins
As Reported by the ACA[57]

	ABC	NBC	CBS	Fox
Shop NBC		•		
Soapnet	•			
Speed				•
Toon Disney	•			
VH1 Classic			•	
VH1 Country			•	

The three retransmission disputes described above, that resulted in broadcast signals being temporarily withheld from MPVD subscribers, all revolved around the pricing and carriage of other cable networks produced by the broadcaster. In the dispute between Cox and Fox, Cox reports that the bargaining impasse was that Fox wanted to increase the license fees of Fox Sports Net by approximately 50% and that Cox relented after Fox withdrew its broadcast signal from Cox.[58] The New York Times reports that ABC was able to extract the following list of concessions as a result of its retransmission consent agreement with Time Warner.

> In return for permission to carry ABC's signals through May 2006, the cable company agreed to convert the Disney Channel by 2003 from a service that viewers have to pay extra for to one that is included in their basic package. It will begin carrying Disney's Toon Disney and SoapNet channels on some of its systems and expand its distribution of Disney's ESPN 2 and ESPN Classic sports networks. Time Warner also agreed to consider adding two unspecified Disney channels, which are currently under development, to some of its systems.[59]

Kagan World Media explains that the Viacom/Echostar dispute was also largely over whether Echostar would carry new programming at the prices that Viacom wanted to charge for it:

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[58] *See* Comments of Cox Enterprises, Inc., MB Docket No. 02-277, at 45 (Jan. 2, 2003).

[59] Jim Rutenberg, "Time Warner and Disney Reach Cable Deal for ABC," New York Times, May 26, 2000, at C6.

> The cable network giant's programming was removed from the DISH Network service for 48 hours starting Mar. 9, 2004, with much of the fracas centering on Viacom's insistence that DISH carry nets it didn't want (Noggin, NICK GAS and Nick Too.) Eventually the two companies worked something out, leading to carriage for all the cable networks. . .[60]

Fortune has described Disney's use of retransmission consent regulations as follows:

> Disney also did a pretty good imitation of Microsoft when negotiating cable carriage with Time Warner. How so? Think of ABC as Windows. It's the No. 1 network, the operating system everyone wants. To get ABC, Disney told Time Warner, you'll also have to pay for a bunch of not-so-hot channels (think of all the applications tied to Windows) that you don't really want: SoapNet, which is mostly repeats of daytime soap operas; Toon Disney, which is repackaged cartoons; and Disney Channel, an also-ran in the Nielsens to Viacom's Nickelodeon and Time Warner's Cartoon Network.[61]

At a recent investors' conference Disney chairman Michael Eisner is quoted as describing Disney's use of the retransmission consent process as follows:

> Without ABC in our own stations, we would not have been able to achieve the major growth we have realized at ESPN and our other cable holdings; because ABC offers the highly valued programming that cable operators need, i.e., retransmission consent.[62]

An article published in the *Wall Street Journal* nicely summarizes the current situation as follows:

> [T]he media giants have discovered that owning both broadcast and cable outlets provides powerful new leverage over advertisers and cable- and satellite-TV operators. The goliaths are using this advantage to wring better fees out of the operators that carry their channels and are pressuring those operators into carrying new and untried channels. . . . . Joint ownership of cable and broadcast is particularly valuable in negotiations with cable operators. A 1992 law allows broadcasters to regularly negotiate the price for carrying TV stations' signal on cable. While broadcasters could charge a cash fee, they usually offer the broadcast stations free in exchange for carrying a new cable channel they've

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[60] *Kagan (2005)* at 9.

[61] *Dumb and Dumber*, Fortune, May 29, 2000, at 140.

[62] *Walt Disney at Citicorp Smith Barney Entertainment, Media and Telcom Conference,* FC Wire, Jan. 6, 2004.

> launched. Few viewers would subscribe to cable if ABC, CBS, and NBC weren't on the channel lineup, so the cable operators have little leverage. The strategy lets broadcasters add more cable channels, including many narrowly focused networks.[63]

In conclusion, there appears to be almost complete and unanimous agreement among industry participants and observers, including the broadcasters themselves, the press, industry analysts, and the Commission, that broadcasters bundle retransmission consent together with other cable programming they produce and use this as a bargaining chip to negotiate some combination of higher license fees and increased carriage than they otherwise would have been able to negotiate.[64]

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[63] Martin Peers, "Show of Strength: How Media Giants Are Reassembling the Old Olipogoply; Mix of Broadcast and Cable Proves Lucrative in Making Deals, Promoting Shows; Playing Hardball With Barbie," Wall Street Journal, September 15, 2003.

[64] To the extent that these effects occur, we would expect a statistical analysis to show that, holding all other factors constant, (i) program networks owned by broadcasters are more likely to be carried by any given cable system than program networks not owned by broadcasters and (ii) program networks owned by broadcasters charge higher license fees than program networks not owned by broadcasters. The GAO conducted an empirical study and found evidence of (i) but not of (ii). *GAO (2003)*. That is, it found that broadcaster owned networks were significantly more likely to be carried by cable systems than non broadcaster owned networks but that they did not charge significantly higher license fees. The GAO findings therefore support the theory that broadcasters exert their monopoly power by forcing additional carriage of their cable networks but do not support the theory that broadcasters exert their monopoly power by charging higher license fees for their affiliated networks. Of course, the harms to consumers would still be significant even if the primary way that broadcasters exercised their market power was to force the carriage of additional networks rather than to raise the license fees that they charge for networks. *See infra*, section IV. However, I believe that the fact that the GAO could not find a license fee effect may well be due to lack of adequate data to measure the desired effect and possible flaws in their empirical methodology rather than because the effect does not exist. I will now briefly list some of the more troublesome issues. First, the accuracy of the GAO conclusion depends on whether it was able to find exogenous variables that would allow it to accurately predict the license fee that a network should sell for in the absence of any extra leverage created by retransmission consent. Given the small amount of data available and the numerous difficult to measure factors likely to affect the value of programming, it is not clear that they were able to successfully do this. Second, financial arrangements associated with the launch of a new cable channel generally involve other payments (often interpreted as payments for promotion) besides license fees and the GAO has no data on these other payments. It may well be that one of the

B. Economic Theory Explains Why The Networks Use Affiliated Program Networks As Currency In Retransmission Consent Negotiations

In this subsection I will provide some economic reasons to explain why the practice of bundling retransmission consent together with MVPD network programming instead of charging a stand alone license fee for retransmission consent has arisen and how the economic motivation for bundling may affect the nature of the resulting consumer harm.

If a broadcaster is suddenly given the opportunity to negotiate compensation for retransmission consent, there are two alternative forms that the compensation could take. The first alternative would be for the broadcaster to simply charge a stand-alone price for retransmission consent. Under this alternative the broadcaster would not raise the license fees it charges for any other network that it produces nor would it require any MVPD operator to purchase any additional MVPD network that it produces. Thus the effects of the exercise of market power would not spill over into the MVPD network programming market and would be easy to measure. Namely, programming costs for the MVPD operator would increase by the amount that the broadcaster charged for retransmission consent. The second alternative would be a form of in-kind compensation for retransmission consent, in which permission to carry a

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major ways that broadcasters exercise their market power over retransmission consent is to negotiate significantly lower (or practically zero) initial payments associated with the launch of new cable networks. Third, one of the best ways to look for evidence of a price effect would be to see if networks are able to charge higher prices to cable operators in regions served by an O&O compared to regions not served by an O&O. However, the GAO only has data on average license fees for the nation as a whole and has no data on the specific license fees that actually paid by individual MSOs. Fourth, the evidence I described above suggests that there may well only be a significant leverage effect for new networks. However, it appears that the GAO looked for an effect that was independent of the age of the network. There may simply not be enough data to attempt to estimate a leverage effect only for new channels. (*i.e.*, there may be too few new channels launched in any given year to perform a meaningful statistical analysis of whether or not new channels launched by broadcasters charge higher license fees than new channels launched by non broadcasters, controlling for other factors that should affect the size of the broadcaster's local stations is conditioned upon carriage of some or all of the MVPD networks that the broadcaster sells. In this alternative, the broadcaster would inform MVPDs that they could only receive retransmission consent if they purchased the specified programming at specified prices.

Note that a broadcaster can generally earn positive profit from being compensated for retransmission consent by obtaining carriage of affiliated networks, even if it does not raise any of the license fees that it charges for its programming, but simply forces more MVPDs to carry the network at the existing prices. This is for two reasons. First, production costs are largely fixed so any extra revenue that the broadcaster earns by forcing more operators to buy the MVPD network is almost completely profit. Second, producers of network programming earn a significant share of their revenue from sales of advertising spots on the network. Advertising revenue will also increase if more MVPDs carry the network. Of course, in reality the broadcaster is likely to find it optimal to raise prices to some extent as well as to require MVPDs to purchase the network who otherwise wouldn't have purchased it.

I believe that there are two economic reasons why we observe bundling in this market and I will now separately discuss each one.[65]

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license fee).

[65] The economics literature identifies two other important reasons why bundling may occur in some markets which I believe are not significant in this market. These are that: (i) bundling can reduce transactions costs if most people would purchase the bundle in any event and that (ii) firms can essentially use bundling to attempt to price discriminate if different consumers have different patterns of demand. The welfare effects on consumers of bundling are likely to be positive if bundling is motivated by (i) and may be positive or negative if bundling is motivated by (ii). *See, e.g.*, William James Adams & Janet L. Yellen, "Commodity Bundling and the Burden of Monopoly," *The Quarterly Journal of Economics*, 51, 475-498 (Aug. 1976); Richard Schmalensee, "Gaussian Demand and Commodity Bundling," *The Journal of Business*, S211-S230 (Jan. 1984); R. Preston McAfee, John McMillan & Michael D. Whinston, "Multiproduct Monopoly, Commodity Bundling, and Correlation of Values," *The Quarterly Journal of*

1. Both Broadcasters and MSOs had reasons to prefer that payment for retransmission consent be made in the currency of agreements to carry program networks rather than stand alone cash payments.

I believe that both sides of the retransmission consent negotiation had some reasons to prefer that payment for retransmission consent be made in "kind" by agreements of MVPDs to carry specified program networks at specified prices rather than payments in "cash" that were explicitly labeled as payments for retransmission consent. The fact the both parties had reasons to view explicitly labeled payments as more "costly" in some sense than payments in kind therefore biased the parties towards using payment in kind rather than payment through a stand alone cash payment.

First, "in kind" compensation in the form of carriage of affiliated networks obscures the fact that retransmission consent essentially results in MVPD subscribers having to pay to watch programming they could view over the air for free. Imagine that an MVPD was paying a license fee of $1 per subscriber per month that was explicitly labeled as a payment for retransmission consent and the operator was called before Congress or the Commission to explain why subscription prices were so high. One justification that MVPD would certainly offer is that it passes the $1 retransmission consent fee through to subscribers, so rates are $1 higher per month than they would otherwise be because his customers are paying to watch signals that they could view for free over the air. Obtaining carriage for affiliated program networks , rather than cash,

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Economics, 104, 371-383 (May 1989); Gregory Crawford, "The Discriminatory Incentives to Bundle: The Case of Cable Television," unpublished manuscript, Duke University (Oct. 7, 2002). The economic motivations that MVPDs have to bundle programming at the retail level are very different than the economic motivations that explain the type of bundling that occurs in the case of bundling of retransmission consent together with cable channels at the wholesale level. In particular I believe that motivations (i) and (ii) likely play a strong role in explaining bundling at the retail level instead of the two motivations I discuss in the text that I believe explain bundling of retransmission consent together with cable channels at the wholesale level.

may in fact strengthen and prolong the broadcasters continued ability to charge for retransmission consent by obscuring the real costs of such transactions.

Second, it may that the Big Four would be put under more pressure to share retransmission consent revenues with program producers if there was a revenue stream explicitly labeled as revenue from retransmission consent. For example, it was widely reported in the press at the time that retransmission consent regulations were first introduced that studios would attempt to negotiate a share of any revenues that networks earned from retransmission consent. [66] A bill was even introduced in Congress to effectively require networks to share retransmission consent revenues with studios.[67] The pressure to share retransmission revenues with program producers may be reduced to the extent that these revenues are kept out of sight.

Third, cable carriage retransmission consent deals may also have been attractive to the major network broadcasters because such arrangements offered them the opportunity to establish

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[66] *See* "Down To The Wire," National Journal, May 16, 1992 ("Valenti argues that [retransmission consent] deals between cable operators and broadcasters would leave his members out in the cold by giving broadcasters control over copyrighted programs. 'We don't oppose a second stream of income for broadcasters,' he told members of the House Intellectual Property Subcommittee. 'But in the name of reason and justice, creative program owners cannot be exiled from their rightful share of royalties.'"); "Don't Count Retrans Bucks Yet," *Variety*, October 5, 1992 ("Hollywood TV distributors, particularly the major studios . . . are writing clauses into contracts for syndicated shows that, in effect, cut the distributor in on any cash a TV station rakes in through retransmission consent."); "Many Players Eye Retransmission Pot," *Broadcasting*, October 12, 1992 ("Although Hollywood and other program providers won't get a direct cut of retransmission-consent fees, its likely that they will be compensated, and the discussions are already under way on how to keep everyone happy. Two studio executives . . . both said they expect some form of compensation from retransmission-consent revenues. Said one: 'It's not that we don't know they've been under pressure. We're aware of the effects of cable on their business . . . We're just saying that we view our programming as the thing that gives them the greatest value, and that's why we would like some compensation.'").

[67] *See* "Hughes Introduces Bill to Force Broadcasters to Pay Copyright Owners," *Communications Daily*, January 7, 1993 ("Broadcasters don't directly own rights to programming they transmit, Hughes said, so they shouldn't be able to sell retransmission rights. 'You should not be able to sell something you don't own.'").

standalone programming assets with recurring license fee and advertising revenue.[68] The combined effect of their in-house libraries of news and entertainment content together with the repeal of the fin/syn restrictions meant that the major network broadcasters could create program network assets at a relatively small incremental cost – using content they had already produced or purchased for broadcast in prime-time and/or shows acquired from their affiliated production studios.[69] In addition, the triennial retransmission consent negotiation required by law meant that broadcasters would have multiple, mandatory bargaining opportunities to obtain the channel

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[68] *See* "ABC Says It Avoided 'Bloody Battle' on Retrans By Not Seeking Money," *Communications Daily*, January 13, 1994 ("It was in Cap Cities/ABC's best interest to avoid [a] 'bloody battle' with [the] cable industry by not seeking money for retransmission consent rights after Cable Act became law and 'the battle didn't seem like it was worth fighting.' Instead, ABC opted to form cable channel ESPN2 (which now is operating) with guaranteed access to cable MSOs and '<u>we've created a real asset</u>' even if regulatory rules change in future, he said: '<u>If you looked at cash for retransmission consent, that could have gone away in the future [and] all of a sudden our hands would be empty.</u>'") (emphasis added). "Newest Cable Act Child: America's Talking," *Variety*, June 27, 1994 – July 3, 1994 (Characterizing America's Talking as one of the "creatures of the Cable Act of 1992, which said in one of its clauses that stations could demand payment from a cable system for picking up and retransmitting their signals. . . . ' The most important function of America's Talking is to create a valuable asset for the NBC network,' said David Zaslav, senior VP of affiliate marketing sales for America's Talking); "7 More Retrans Deals Boost NBC Cable Channels," *The Hollywood Reporter*, September 15, 1993, ("These agreements further solidify the position of CNBC in the cable marketplace and enhance NBC's opportunity to build a new cable programming asset for the future," said NBC cable and business development president Tom Rogers").

[69] *See* "Seinfeld," *Business Week*, June 2, 1997 ("When NBC launched its MSNBC cable and Internet joint venture with Microsoft, it was at almost no real cost to the network. It had acquired hard-to-get carriage on cable systems as part of its retransmission consent negotiations with cable operators and had launched a low-rated chat channel, America's Talking. . . Launched less than a year ago, it has tiny ratings and is not yet turning a profit. But because it reaches 35 million homes, MSNBC has an asset value of about $1 billion"); "Davatzes Works to Bring A&E Back to Where It Once Belonged," *Broadcasting and Cable*, June 9, 2003 ("NBC can repurpose shows on Bravo and use retransmission consent to build out Bravo's distribution").

capacity and carriage terms needed to establish and/or grow their standalone program network assets.[70]

Fourth, cable operators may have perceived that they would be able to lower their effective payments to broadcasters not owned by the Big Four by paying the Big Four for retransmission consent in a "currency" that was of little value to other broadcasters. In particular, if cable operators had negotiated cash payments for retransmission consent with the major networks, it was possible that other broadcasters would have insisted on being paid similar cash payments. The advantage of agreements to carry other program networks produced by the networks was that most other broadcasters could not simply insist on receiving the same sort of deal because they did not produce program networks.[71] It was widely reported at the time of the initial retransmission consent negotiations that the retransmission consent agreements that cable operators negotiated with the four major networks would serve as a blueprint for subsequent agreements that other broadcasters would be able to negotiate with cable operators and that independent broadcasters were extremely disappointed when the retransmission agreements negotiated by the networks on behalf of their O&O's arranged for payment in the form of

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[70] *See* "Looking Back At Retransmission," *Electronic Media*, March 4, 2002 ("But by and large, broadcast station representatives said retransmission consent turned into a tool for the broadcast networks to beef up their presence in the cable industry, a tool that has hurt the interests of broadcasting by moving to cable funds from the networks that could have been used to improve broadcast programming. They [the networks] did create assets for the '90s that appreciated, but not for the affiliates," said Post-Newsweek's Mr. Frank"); "Karmazin to Play Retrans Chip for MTVN Cable Nets," *Multichannel News*, May 22, 2000 (Frank Hughes, senior vice president of programming for the National Cable Television Cooperative, which represents small and midsized MSOs, said that nowadays, "It's like companies buy up all of these cable assets to do retransmission consent.").

[71] *See, e.g.*, "Retrans Weaves New Webs," *Variety*, July 26, 1993 – August 1, 1993 ("But taking on another channel may not be the best solution for a station seeking to climb out of the thicket of retransmission consent. 'A lot of network affiliates have trouble programming their one station,' says John Rohr, VP and director of programming for Blair TV, the rep firm").

agreements to carry cable network programming produced by the networks instead of cash.[72] There are also recent articles in the trade press that suggest that the bargaining position of independently owned broadcast stations was negatively impacted by the fact that networks and MVPDs agreed to carriage of cable network programming in exchange for retransmission consent.[73]

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[72] *See* "Cable, Stations New Link Gets Clear Reception," *Daily Variety*, April 1, 1993 ("An early blueprint for the negotiations between cable operators and TV stations may emerge out of the talks now going on between the big MSOs like TCI and Time Warner and the stations owned and operated by the four networks. 'Everyone is keeping these negotiations under wraps,' says Harry Pappas, who owns Fox affiliates in Fresno and Omaha. 'But what comes out of these discussions may serve as a kind of model that the rest of the network affiliates will follow.'"); "Carriage Fee Battle Heating Up," *Electronic Media*, May 3, 1993 ("FBC affiliates sounded the alarm at word that their network was trying to cut a group deal with Tele-Communications, Inc. and other MSOs that would give Fox a second cable channel to program in local markets in lieu of cash fees."); "Affiliates Question ABC Deal," *Electronic Media*, July 19, 1993 ("A number of broadcasters expressed anger and frustration last week at the retransmission consent deals that Capital Cities/ABC and the Hearst Corp. reached with Continental Cablevision. Most vocal were ABC affiliates, which said their positions at the bargaining table will be hurt by Hearst and ABC's acceptance of a rollout of their ESPN2 in lieu of straight cash."); "CBS, Cablers Playing Chicken," *Hollywood Reporter*, July 20, 1993 ("ABC's deal with Continental Cablevision indicates an enormous value being placed on ABC stations. However, ABC's deal leaves affiliates out in the cold. [CBS's] Kreigel said, because it calls for a national rollout of ESPN2 in exchange for retransmission consent of only ABC O&O stations. 'The most serious question in the ABC deal is what they've done to their own affiliates,' he said.").

[73] *See* 'Smulyan: Retrans or Bust," *Broadcasting and Cable*, December 16, 2002 ("The major media companies, though, leveraged their retransmission rights into MSO support for new cable programming services. ABC launched ESPN2 that way, while NBC and Microsoft launched News Channel MSNBC, and News Corp. developed FX. And some broadcasters believe those initiatives crushed any hope they had of getting cash for their broadcast signals. 'That really created a great value shift' away from broadcast television to cable TV, explained LIN Television Chairman Gary Chapman. 'It undermined our ability to get paid for our broadcast signals.'"). To the extent that this strategy has been successful in minimizing payments to local broadcasters other than the network O&Os, it may be the case that the primary beneficiaries of retransmission consent regulations have been the four major networks, and that the benefits received by independently owned local broadcasters have been relatively modest. For example, Electronic Media quotes some local broadcasters as suggesting that "the major parties to benefit form the regulations [are] the Big 4 TV networks." "Looking Back At Retransmission," *Electronic Media*, March 4, 2002.

Fifth, cable operators may have preferred that payments for retransmission consent be labeled instead as payments for network programming, at least in the era when the prices of cable firms were regulated, because these regulations made it easier to pass through to subscribers cost increases for new programming added to the expanded basic tier. When retransmission consent regulations were put in effect in 1992 and continuing until 1999, both the basic and expanded service tiers were regulated. The price of the basic tier was regulated by local franchise authorities while the price of the expanded basic tier was regulated by the Commission. The press reported at the time of the initial retransmission consent negotiations that MVPDs were concerned that local franchising authorities might balk at allowing price increases to pass through the costs that MVPDs incurred that were explicitly labeled as payments for retransmission consent.[74] In fact, Commission rate rules expressly provided that in the first year of retransmission consent, any cash payments required for carriage of local broadcast stations could not be passed through to subscribers. By contrast, the chances of obtaining Commission approval for pass through of cost increases for new program networks added to expanded basic were much higher. In fact, in 1994 - partially in response to concerns that rate regulation had chilled new programming investment in all service tiers - the Commission adopted a set of "going forward" rules aimed at facilitating the introduction of new program channels. Those rules allowed cable operators to recover twenty cents per channel per month for each program

[74] *See* "Don't Count Retrans Bucks Yet," *Variety*, October 5, 1992 ("Part of the problem, says TCI's Bob Thomson, VP of government affairs, is the added expense that cable subscribers would be forced to pass on to consumers (assuming the government allows operators to boost subscriber bills). 'There's no way we could explain to our customers or to local city councils that we'd have to jack up monthly rates to our subscribers for TV stations they could get free over the air if they didn't subscribe to cable,' he says.")

channel added to the expanded basic tier along with the full amount of the license fee associated with each added channel.[75]

Of course rate regulation of the expanded basic tier ended in 1999, although the basic tier continues to be regulated at the local level. Therefore, to some extent, the motivation of MVPDs to re-label payments for retransmission consent as payments for cable programming may have been reduced in 1999. However, the historic precedents set by past agreements may still have a large influence on the behavior we see today. Furthermore, it may be that making payments that are explicitly labeled as payments for retransmission consent would still cause cable operators some regulatory heartburn today. In theory, cable operators could simply avoid the regulatory process at the local level altogether and respond to an increase in retransmission fees by raising the rates for expanded basic and not bothering to submit a rate case at the local level. However, to the extent that consumer groups could argue that the cable firms were thereby "circumventing" the regulatory process, this might still create political problems for cable operators.

In summary, both broadcasters and MVPDs may have some reasons to prefer that payments for retransmission consent be made in kind instead of in cash. They may have perceived that this would give them bargaining advantages either with one another or with other parties and there may also have been advantages to one or both of them of keeping these payments out of sight by relabelling them as payments for cable network programming. This may at least partially explain why broadcasters and MVPDs have adopted the practice of

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[75] Under this theory, it would have been particularly attractive to bundle retransmission consent with new cable programs rather than cable programs the operator was already showing. As discussed above, this is generally what occurred.

bundling negotiations over retransmission consent together with negotiations over cable network programming.

2. Conditioning Retransmission Consent on Carriage of Affiliated Program Networks As Strategic Foreclosure

It is possible that a firm with market power in one good can "leverage" this market power into other related goods by bundling them together. The issue of whether there can be such a leverage effect has historically been somewhat controversial in the economics literature. In particular, the "Chicago school" argued that there could be no such leverage effect because a firm should always be able to extract the full return from its market power over a good by charging a higher price for that good.[76] In a paper written in 1990, Michael Whinston presented a series of formal models that showed that these arguments implicitly depended on the assumption that there were constant returns to scale in the market for the tied good.[77] In particular, he showed that where there are economies of scale in the market for the tied good, tying can indeed be a profitable strategy for a firm with market power. The argument is that by foreclosing a large part of the market to potential entrants, the firm prevents them from entering or at least considerably weakens them. It is now a well-accepted principle in the theoretical industrial organization literature that when there are significant economies of scale in the market for a good, that a firm with market power over a related good may be able to use bundling to profitably foreclose competitors.[78]

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[76] *See, e.g.*, Aaron Director & Edward H. Levi, "Law and the Future: Trade Regulation, 51 Nw. U. L. Rev. 281, 281-296 (1956); Richard Posner Antitrust Law: An Economic Perspective," Chicago, University of Chicago Press, at 173 (1976). *See also* Whinston *infra* note 77 for further references.

[77] Michael Whinston, "Tying, Foreclosure, and Exclusion," *American Economic Review*, 80(4), September 1990, 837-859.

[78] For example, a recently published paper in this literature summarizes the current state of

Of course, the nature of economies of scale in the market for program networks is extreme. Almost all of the costs in the MVPD network industry are the fixed costs of producing the programming. It is almost costless to distribute the programming to more MVPDs once it is produced. New networks struggle for survival by attempting to achieve a large enough sales base to cover their fixed costs of production. This is precisely the sort of market where we would expect the foreclosure motive to be most important. Therefore, it seems likely that an additional motivation that broadcasters may have to bundle retransmission consent together with other network programs is to capture larger market shares from their potential competitors and thereby either foreclose them from entering entirely or at least weaken them.

The Commission itself, has concluded that bundling and tying to foreclose competitors might well be a real concern in the market for video programming.

> Some of the sales methods discussed, in combination with various regulatory and technological constraints, may cause harms in the market for video programming. Further, some of these harms may carry through to the retail market and adversely affect consumers. In particular, there is some concern that non-affiliated program networks may not be able to gain widespread carriage due to the industry practice of tying carriage of popular program networks or broadcast stations with carriage of less-popular program networks.[79]

Networks themselves have often explained their decision to launch new networks as revolving around this sort of strategic consideration. Namely, network companies have

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knowledge in the field as follows. "In an important article, however, Whinston (1990) has shown that criticisms of the foreclosure argument depend on the tied market being characterized by perfect competition and constant returns to scale and that, given economies of scale and imperfect competition, tying can increase monopoly profitability." Dennis W. Carlton & Michael Waldman, "The Strategic Use of Tying To Preserve and Create Market Power In Evolving Industries," *Rand Journal of Economics*, 33, at 195 (Summer 2002). *See also* Carlton and Waldman (2002); Barry Nalebuff, "Bundling as an Entry Barrier," *Quarterly Journal of Economics*, CXIX, at 159-188 (Feb. 2004), for other models of bundling and tying to deter entry and further references to the literature.

[79] *See A La Carte Report* at 80.

consistently explained that new program networks were going to be launched regardless of whether they entered the program network industry and their efforts to launch new channels were simply designed to insure that, if viewership and advertising dollars migrated to cable, they would not be entirely lost. Demanding carriage of affiliated networks as consideration for retransmission consent ensures that the revenues from these new channels would accrue to themselves instead of their competitors.[80] Rupert Murdoch has used just such an argument in an effort to reassure Fox network affiliates concerned that Fox's investment in affiliated cable channels would cannibalize the core broadcasting business:

> Some of you remain uneasy about our moves into other media. Like it or not, new competition to broadcasting is inevitable. More channels and more video products to compete with broadcasting are coming," Murdoch warned. "They cannot be stopped. We ignore that reality at our own peril. Fox and Fox affiliates are far better served by meeting the marketplace challenge through expansion into complementary media and integration of those media operations to the benefit of our core business broadcasting.[81]

By contrast, independent program networks have expressed concern that the bundling strategies of the four major broadcast networks have impeded their ability to compete in the cable programming marketplace,[82] thereby suggesting that the use of retransmission consent to gain

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[80] *See* "Fox Woos Affils On Retrans," *Variety*, June 4, 1993 ("Affiliates, who voiced concerns about the cable service competing with their programming, also seemed to accept Fox's contention that it would be significantly less prominent than Fox Broadcasting. . . .'If by not launching this new channel, we could assure you that we and you would face no new competition (from cable), then this question would make a lot of sense, [Fox executive] Padden said. He added that the reality is broadcasters are 'powerless' to prevent the spread of new services, but the cable channel will be 'competitive by cable standards, (but) will not pose a threat to our audiences.'").

[81] "Fox Rallies Troops," *Variety*, January 13, 1997 (quoting Murdoch speech to affiliates).

[82] For example, in the Commission's *A La Carte Inquiry*, Discovery Communications, one of the major independent cable programmers, stated that "[retransmission consent] negotiations effectively require carriage of broadcaster-affiliated networks that distributors otherwise would not carry. As a result, many networks not affiliated with broadcasters are excluded from carriage on operators' systems. . . In the Manhattan market, Discovery has been unable to gain carriage

carriage for new program networks has helped to forestall the diversion of revenues and viewership away from the aggregate programming (broadcast + cable) of the network conglomerates. Thus, "bundling" retransmission consent might be used by broadcasters as a means to preserve and defend their existing position and ensure that cable programming does not provide a foothold for competition.

IV. CONSUMERS HAVE BORNE HIGH SOCIAL COSTS BECAUSE OF THE EXERCISE OF RETRANSMISSION CONSENT

There is considerable evidence that the Big Four networks possess market power with respect to their broadcast signals. There is essentially universal agreement among industry participants and observers, including the Big Four themselves, industry analysts, the press, and the Commission, that the Big Four bundle retransmission consent together with program networks that they also produce in order to force MVPDs to (1) pay higher prices for program networks that they might have purchased in any event and (2) purchase additional program networks that they would not have otherwise purchased.

Subscribers to MVPDs are harmed by broadcasters' exercise of market power regardless of whether it occurs through broadcasters charging higher license fees for programming or through broadcasters forcing cable operators to purchase additional programming.

First, consider the effect of higher license fees. Since license fees are charged on a per subscriber per month basis, the MVPD views the per subscriber per month fee as a marginal cost of providing service to the customer. It is of course standard economic theory that a firm facing

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on the expanded basic level of service of either Animal Planet or the Travel Channel, two of Discovery's leading and consistently highly rated networks. The vast majority of channel capacity on the tier is taken up the operator's need to carry other programming, almost 60 percent of which is broadcast affiliated." *Ex Parte* Letter of Discovery Communications (Oct. 18, 2004).

a downward sloping demand curve (as MVPDs surely do) will respond to an increase in its marginal cost by increasing price.

Second, consider the issue of requiring MVPDs to purchase specified programs that they would otherwise have not purchased. To the extent that MVPDs do not automatically reduce the amount of programming that they purchase from other programmers by a compensating amount, once again the total programming costs of MVPDs will rise, and we can expect these increases in programming costs to be passed along to consumers. However, the harms to consumers are likely to be substantial even if MVPDs respond to broadcasters' demands that they purchase more programming by cutting back on the ir purchases from non broadcasters.

Most importantly, this will likely damage competition by either preventing the entry of competitors or at least weakening them. As I discussed in the last section, this may well be one of the primary motives for bundling in the first place. As well, if MVPDs would purchase certain programs from non-broadcasters in the absence of bundling and bundling changes these decisions, then consumers will be worse off because they will be receiving programming that does not meet their needs as well.

My conclusion is consistent with the Commission's findings in its evaluation of the News Corp./DirecTV merger. There, the Commission concluded that consumers would be harmed if News Corp. were to exercise any increase in market power by raising programming prices and/or forcing MVPDs to purchase additional programming.[83]

[83] The FTC also concluded that increases in programming prices would result in increases in prices charged to consumers in its analysis of the Time Warner/Turner merger. *See Time Warner, Inc., et al., Proposed Consent Agreement with Analysis To Aid Public Comment*, 61 Fed. Reg. 50301, 50309 (rel. Sept. 25, 1999) ("The complaint alleges . . . that substantial increases in wholesale programming costs for both cable systems and alternative service providers - including direct broadcast satellite service and other forms of non-cable distribution -

> When News Corp. secures carriage of other cable programming networks from MVPDs in exchange for its broadcast signal, MVPDs pay for those networks. If News Corp. can secure carriage of more cable networks and charge higher fees for such carriage, these fees are unlikely to be absorbed solely by the MVPDs, but would be passed on to consumers in the form of higher rates. If News Corp. uses withholding or threats of withholding in retransmission consent negotiations to obtain carriage of its affiliated cable networks that the MVPD, absent the threat of foreclosure, would not agree to carry, consumers are harmed because MVPDs are forced to make programming decision based on News Corp.'s demands rather than selecting the programming of their choice.[84]

Thus, consumers are harmed when the Big Four exercise market power through the retransmission consent negotiation process to raise license fees on channels that programmers would have purchased in any event or to force them to purchase channels that they otherwise would not have purchased.

There have been concerns raised in the policy community and in Congress that cable prices are too high and that high programming costs have played a major role in causing this problem. Furthermore, there is concern both that license fees for individual cable channels are too high and that perhaps too many new channels have been launched and included in the expanded basic package that subscribers must purchase. Retransmission consent has contributed to these problems by giving broadcasters the incentive and opportunity to ask for payment for retransmission consent by (1) charging higher prices for cable channels and (2) requiring MSOs to launch new channels that they might otherwise not have launched.

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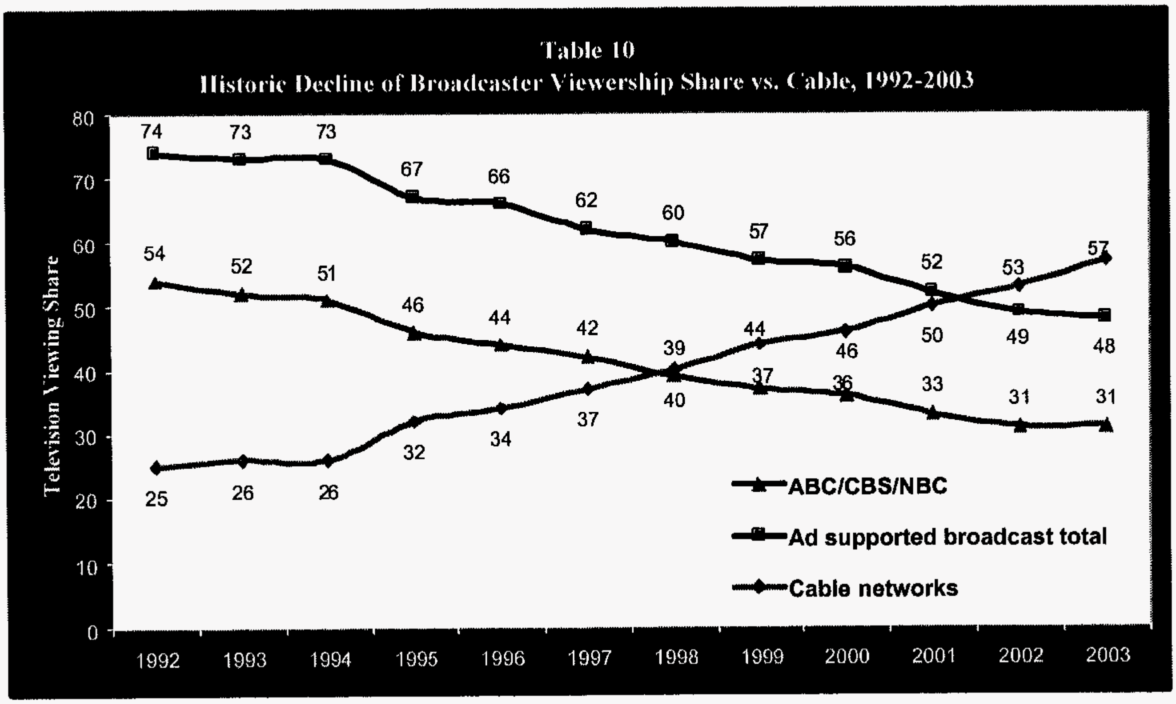
would lead to higher service prices and fewer entertainment and information sources for consumers.").

[84] *News Corp./DirecTV Merger Order* at ¶ 209.

V. THE POTENTIAL SOCIAL BENEFITS OF RETRANSMISSION CONSENT REMAIN UNPROVEN

Fundamentally, Congress hoped that providing broadcasters with a second revenue stream would make it more likely that broadcasters could compete more effectively with cable and that broadcast program quality would increase. However, it is theoretically unclear whether or not retransmission consent regulations would create significant social benefits of the sort Congress had in mind when it introduced these regulations. Moreover, there is no empirical or other factual evidence of any sort that I am aware of that it has in fact produced significant benefits. In fact, even though Congress intended to strengthen broadcasting, fewer and fewer viewers tune into broadcasters every year:



Source: *Kagan (2005)* at 46.

On a theoretical level, it is not clear that simply giving broadcasters an extra revenue stream will increase the amount of money they invest in programming. When broadcasters are given an extra revenue source, it is reasonable to believe that they will use this revenue in a way that will maximize its value to their shareholders. Possible alternatives for the revenue include investing in broadcast programming, investing in some other aspect of their media business (including their cable channels), or paying dividends to shareholders and allowing them to invest the money elsewhere. Therefore, the fact that retransmission consent regulations give broadcasters an extra revenue stream in no way automatically guarantees that they will devote more resources to improving program quality. The real issue is how retransmission consent regulations affect the incentive of broadcasters to invest in programming, not whether or not they give broadcasters more revenue that they could theoretically invest in programming if they wished to.

In fact, somewhat ironically, it may well be that much of the extra revenue stream provided to broadcasters by retransmission consent policy has actually been used to finance the development of the chief competitor to broadcasting -- MVPD program networks. For example, *Electronic Media* reports the view of some local broadcasters that "retransmission consent [has] turned into a tool for the broadcast networks to beef up their presence in the cable industry, a tool that has hurt the interests of broadcasting by moving to cable funds from the networks that could have been used to improve broadcast programming."[85] It has also been reported that Disney uses the nationwide platform the ABC broadcast network gives it to push its stable of *cable*

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[85] "Looking Back At Retransmission," *Electronic Media*, March 2, 2002.

programming interests and does not view ABC itself as a "stand-alone brand" worth promoting.[86]

In Table 11, I present data on the programming expenditures of the broadcast networks and MVPD program networks since 1993 and projections of their future expenditures through 2012. While expenditures of both broadcast and non-broadcast programmers are generally rising, expenditures of non-broadcast programmers have risen at and are predicted to continue rising at a much faster rate than expenditures of the broadcast networks. Therefore the over-all share of programming expenditures devoted to broadcast programming has been falling constantly since 1993 and is projected to continue to fall through 2012.

Table 11
Historic and Projected Programming Expenditures
by Broadcast Networks and National Program Networks[87]

Year	Programming Expenditures (Mil $)					Percentage of Total	
	Broadcast	% Change	Cable	% Change	Total	Broadcast	Cable
1993	5,743		2,198		7,941	72.3	27.7
1994	6,396	11.4%	2,475	12.6%	8,871	72.1	27.9
1995	6,775	5.9%	2,986	20.6%	9,761	69.4	30.6
1996	8,017	18.3%	3,677	23.1%	11,694	68.6	31.4
1997	8,437	5.2%	4,705	28.0%	13,142	64.2	35.8
1998	9,122	8.1%	5,460	16.0%	14,582	62.6	37.4
1999	9,674	6.1%	6,445	18.0%	16,119	60	40
2000	11,203	15.8%	7,265	12.7%	18,468	60.7	39.3
2001	10,848	-3.2%	8,024	10.4%	18,872	57.5	42.5
2002	11,403	5.1%	9,072	13.1%	20,475	55.7	44.3
2003	11,185	-1.9%	10,413	14.8%	21,598	51.8	48.2
2004	12,170	8.8%	11,599	11.4%	23,579	51.2	48.8
2005	11,680	-4.0%	12,862	10.9%	28,563	44.8	55.2

[86] *See* Charles Dubow, *Clarification: Eisner Discusses the ABC Brand and Other Disney Brands*, Nov. 13, 2002, *available at* http://www.forbes.com/2002/11/13/cx_cd_1113disney.html.

[87] *Kagan (2004)*.

Year	Programming Expenditures (Mil $)					Percentage of Total	
	Broadcast	% Change	Cable	% Change	Total	Broadcast	Cable
2006	12,946	10.8%	14,255	10.8%	27,201	47.6	52.8
2007	12,800	-1.1%	15,763	10.6%	28,563	44.8	55.2
2008	13,960	9.1%	17,308	9.8%	31,268	44.6	55.4
2009	13,261	-5.0%	18,839	8.8%	32,100	41.3	58.7
2010	14,661	10.6%	20,458	8.6%	35,119	41.7	58.3
2011	14,533	-0.9%	21,967	7.4%	36,500	39.8	60.2
2012	15,766	8.5%	23,521	7.1%	39,287	40.1	59.9
% change 1993-2004		**111.9%**		**427.7%**	**196.9%**		
% change 1993-2012		**174.5%**		**970.1%**	**394.7%**		

Of course, it is possible to make the claim that the share of total programming expenses devoted to broadcasting would have fallen even faster if retransmission consent regulations had not been in place. To prove such a claim one would have to conduct a statistical analysis of the determinants of programming expenditures and show that programming expenditures of the broadcast industry appear to have been larger than they would otherwise have been since 1993. I am aware of no such study.

Available evidence certainly does not suggest that the quality of broadcast programming has increased since the passage of the Cable Act in 1992 either in absolute terms or relative to cable programming. For example, networks have attempted to reduce their production costs by showing a much greater share of reality programming and game shows which are cheaper to produce than other types of programming. Table 12 presents the number of hours of various types of programming shown by the four major broadcast networks in 1992 and 2004. The major change is that "unscripted" programming (which is primarily reality shows and game shows) has grown dramatically more important primarily at the expense of movies. Indeed, according to information provided by Viacom in the Commission's media ownership proceeding, reality television has *tripled* as a percentage of the major networks' prime-time schedules from 1995 to 2003.[88] Arguably, this sort of programming was not what Congress intended to support when broadcasters were given additional revenues from retransmission consent. There is of course considerable debate as to whether an increase in this genre represents enhanced quality.

Table 12
Change in Hourly Prime-time Big Four Broadcast Programming, 1992-2004[89]

	1992		2004		
	Hours	% Total	Hours	% Total	Change in Hours, as %
Unscripted	10.5	13.1%	21.5	26.5%	**104.8%**
Comedy/Drama	44.5	55.6%	43	51.9%	-5.6%
Movies	14	17.5%	4	4.9%	**-71.4%**
Newsmagazines	6	7.5%	9.5	11.7%	58.3%
Specials	5	6.3%	4	4.9%	-20.0%

Table 13 shows the number of Emmys won by broadcast vs. cable programs over the period 1992-2003. In 1992 broadcast TV won the vast majority of Emmys but by 2003 they are split more evenly between TV and cable.

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[88] *See* Opening Statement for David F. Poltrack, Executive Vice President, Research and Planning, CBS Television, at the Forum on Media Ownership Rules, Columbia University Law School, January 16, 2003, at p. 3, attached to Letter from John C. Quale to Marlene Dortch, Jan. 22, 2003, MB Docket 02-277, MM Docket 01-235, MM Docket 01-317, MM Docket 00-244.

[89] "Broadcasting's Ratings Week July 6-12," *Broadcasting*, July 20, 1992, at 18; *Nielsen Ratings*, Broadcasting & Cable, July 19, 2004, at 18. A.C. Nielsen considers "prime-time" viewing hours as between 8pm and 10:30pm Monday through Saturday, and 7pm to 10:30pm on Sundays. "Unscripted programs" include reality television shows, game shows, and programs that replay clips or reenactments of home video or police footage. "Movies" are ninety minute or two hour broadcasts of feature films or made-for-television films. "Newsmagazines" describe in-depth investigative series or documentaries, as local news broadcasts are not shown during prime-time. "Specials" describe broadcast coverage of infrequent events, such as the Olympics

Table 13
Big Four Broadcast and Cable Prime-time Emmys, 1992-2003[90]

	1992	1997	2000	2003	% Change
Broadcast	60	53	56	47	**-21.6%**
Cable	11	28	26	39	**254%**

VI. CONCLUSION

The four major national broadcast networks use retransmission consent regulations to negotiate significant compensation from MVPDs in return for giving them permission to retransmit the signals of their owned and operated broadcast stations. These costs are passed on to MVPD subscribers in the form of higher subscription prices. Consumers also are harmed because these tie-ins reduce competition in the market for network programming and distort the selection of programs that is available to MVPD subscribers. Because there is no simple transparent measure of the harm to consumers, the costs of this policy are somewhat hidden. Nonetheless they are likely significant and should be considered in any over-all evaluation of the social value of retransmission consent rules.

The potential benefits of retransmission consent rules on broadcasting remain largely unproven and unmeasured. In fact, somewhat ironically, it may well be that much of the extra revenue stream provided to broadcasters by retransmission consent policy has actually been used to fund cable programming which is the major competitor to over-the-air broadcasting.

Given that retransmission consent policy appears to create significant social costs and given that the social benefits of this policy are not readily apparent, I conclude that policymakers

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or an awards show. "Comedies and dramas" are scripted programs with recurring casts.

90 Academy of Television Arts & Sciences, Advanced Primetime Awards Search, *available at* http://www.emmys.org/awards/awardsearch.php

should attempt to more carefully investigate whether or not there are any social benefits to this policy, with an eye towards changing the policy unless evidence can be found that significant social benefits exist that outweigh the social costs.

I declare that the foregoing is true and correct:

Bill Rogerson

William P. Rogerson

Dated:

February 28, 2005

February 2005

Curriculum Vitae

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Earl C. Anthony Fellowship, 1976-77
Canada Council Doctoral Fellowship, 1979-80
Shelby Cullom Davis Fellowship, 1979
NSF Grant SES-8320451, "Moral Hazard, Reputation, and Product Quality,"
March 1984 - March 1985
NSF Grant SES-8504304, "Moral Hazard, Reputation, and Product Quality,"
April 1985 - September 1987
NSF Grant IRI-8705477, "Contracting Under Asymmetric Information,"
July 1987 - December 1989Named to Household International Professorship in Economics, September
1987 - August 1989
Lynde & Harry Bradley Foundation Research Grant, "An Economic Analysis

of Defense Procurement Regulations," June 1989 - December 1991.
NSF Grant SES-8906751, "Profit Regulation of Defense Contractors," August 1, 1989 - July 31, 1991.
Olin Fellow at The Center for the Study of the Economy and the State, University of Chicago, October 1, 1989 - June 30, 1990.
Smith Richardson Foundation, Inc. Research Grant, "Economic Incentives and the Defense Procurement Process," March 1, 1993 - May 31, 1995.
Elected a Fellow of the Econometric Society, 1999.
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Research and Teaching Interests

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Employment History

Research Assistant to Canadian Member of Parliament, Arnold Malone, June 1975 - September 1975
Teaching Assistant at University of Alberta, September 1975 - June 1976
Economist, Department of Industry, Trade and Commerce, Government of Alberta, June 1976 - September 1976
Research Assistant, Environmental Quality Laboratory, Caltech, June 1977 - September 1977
Economist, Long Range Planning and Structural Analysis Division, Department of Finance, Government of Canada, June 1978 - September 1978
Teaching Assistant to Professor Charles R. Plott, Division of Humanities and Social Sciences, Caltech, September 1979 - June 1980
Assistant Professor of Economics, Stanford University, September 1980 - August 1984
Associate Professor of Economics, Northwestern University, September 1984 - May 1990
Professor of Economics, Northwestern University, May 1990 - Present
Chair, Economics Department, Northwestern University, September 1996 - August 1998.
Chief Economist, Federal Communications Commission, June 1, 1998-May 31, 1999 (on leave from Northwestern for this year.)
Director, Northwestern Program in Mathematical Methods in the Social Sciences, September 2000- present.

Professional Activities

Editor of Defense and Peace Economics, January 1995 - December 1998.
Member of the editorial board of Defense and Peace Economics, September 1991 - December 1998.
Member of the editorial board of Review of Accounting Studies, September 1993 to September 2004.
Member of the editorial board of Journal of Industrial Economics, October 1995- Sept. 1998.
Chief Economist of Federal Communications Commission, June 1, 1998 - May 31, 1999.
Member of the Illinois Economic Policy Council, September 1999 to September 2000
Director, Northwestern Program in Mathematical Methods in the Social Sciences, September 2000- present.
Member of Northwestern's Program Review Committee, September 2000 - June 2003.
Chair of Northwestern's Program Review Committee, September 2002 - June 2003.
Co-Director, Center for the Study of Industrial Organization (CSIO), September 2001- present.
Consultant to: Federal Communications Commission, Federal Trade Commission, Institute for Defense Analysis, Logistics Management Institute, Office of the Secretary of Defense (Program Analysis and Evaluation), RAND Corporation, US Department of Justice.

Refereed Publications

"Aggregate Expected Consumer Surplus As a Welfare With an Application to Price Stabilization," Econometrica, 49, No. 2, (March 1980), pp. 423-436.
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